Federal Arbitration Act, 9 U.S.C. § 2:

> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

STATEMENT OF THE CASE

This Petition requests this Court's review of the Montana Supreme Court's decision in one of twenty-three actions[3] against Piper Jaffray that allege generally that a former Account Executive, Mr. O'Neill, in Piper Jaffray's branch office in Butte, Montana had engaged in improper conduct with respect to accounts of plaintiffs in each of the twenty-three lawsuits.[4]

Respondents here are husband and wife who opened eight accounts with Piper Jaffray. Respondent husband previously worked on Wall Street for six years, and currently works as a physician in Butte, Montana. (App. 32-34). Each Respondent individually opened three accounts,

---

[3] The twenty-three lawsuits, and the status of each, may be found in the Appendix at 76.

[4] On January 12, 2005 Mr. O'Neill pled guilty to two counts of unauthorized trading in the accounts of two (2) clients with whom Piper Jaffray has reached settlements. Mr. O'Neill was sentenced on April 29, 2005. He is required to make restitution to Piper Jaffray in the amount of $308,000, representing amounts which Piper Jaffray paid into a restitution fund as part of the settlement with the Montana Auditor's Office and Securities Department arising out of O'Neill's and Piper Jaffray's alleged misconduct.

two IRA accounts and an individual account; Respondents together opened a joint account; and Respondent husband opened one account in the name of Montana Facial Surgery.

Respondents executed seven account agreements containing pre-dispute arbitration provisions. (These agreements signed by the Respondents are collectively referred to as the "Account Agreements.") The pre-dispute arbitration provisions conform to the language required by the securities self-regulatory organizations, the New York Stock Exchange, Inc. ("NYSE") and the National Association of Securities Dealers, Inc. ("NASD"), and are typical of arbitration provisions found in virtually every customer account agreement used in the securities industry throughout the United States.

For example, three of the four IRA agreements ("IRA Agreements") executed by Respondents provide, in pertinent part:

> .... **I agree to arbitrate any disputes between Piper Jaffray and me. I specifically agree and recognize that all controversies which may arise between Piper Jaffray, its agents, representatives or employees and me, concerning any transaction, account or the construction, performance or breach of this or any other agreement between Piper Jaffray and me, whether entered into prior, on, or subsequent to the date hereof, shall be determined by arbitration to the full extent provided by law....**

(Bold in original).[5] The IRA Agreements also confirm Respondents' receipt of the IRA Agreement and acknowledgement of the arbitration clause in words which appear

---

[5] The complete arbitration provision contained in the IRA Agreements may be found at App. 72-73.

immediately above Respondents' signatures: "**I UNDERSTAND THIS AGREEMENT CONTAINS A PRE-DISPUTE ARBITRATION CLAUSE AT PARAGRAPH 4 ABOVE, AND I ACKNOWLEDGE RECEIPT OF A COPY OF THIS AGREEMENT.**" (Bold, all capital lettering in original document).

Respondents also agreed to arbitration in four other account agreements. In Respondents' individual account agreements, joint account agreement, and the account agreement in the name of Montana Facial Surgery ("Non-IRA Agreements"), Respondents entered into a contract with Piper in which they agreed that any disputes would be resolved through arbitration. The arbitration clause employed in these agreements is almost identical to that contained in the IRA Agreements, and in pertinent part provides:

> **. . . You agree to arbitrate any disputes between Piper Jaffray and you. You specifically agree and recognize that all controversies which may arise between Piper Jaffray, its agents, representatives or employees and you concerning any transaction, account or the construction, performance or breach of this or any other agreement between us, whether entered into prior, on, or subsequent to the date hereof, shall be determined by arbitration to the full extent provided by law. . . .**

(Bold in original).[6]

As with the IRA Agreements, these Non-IRA Agreements also contain the Respondents' written confirmation of receipt of a copy of the agreement and acknowledgement of the arbitration provision immediately above the signature line:

---

[6] The complete arbitration provision contained in the account agreement may be found at App. 74-75.

> **BY SIGNING THIS AGREEMENT YOU:**
>
> . . . .
>
> **2. UNDERSTAND THIS AGREEMENT CONTAINS A PRE-DISPUTE ARBITRATION CLAUSE AS SHOWN ON PAGE 7, PARAGRAPH 12.**
>
> **3. ACKNOWLEDGE RECEIPT OF A COPY OF THIS AGREEMENT.**

(Bold and all capital lettering in original document). The remaining IRA account agreement, signed by Respondent wife, does not contain an arbitration provision, however, Respondent wife subsequently signed three account agreements (an IRA, an individual account, and a joint account) containing the arbitration agreements listed above agreeing to arbitrate "any" dispute concerning "any" account or breach of "any" agreement with Piper Jaffray.

When each plaintiff in the twenty-three lawsuits initiated litigation, Piper Jaffray demanded each plaintiff, including the Respondents here, to submit the dispute to arbitration. Every plaintiff refused to arbitrate, and Piper Jaffray then moved the state district court to compel arbitration. After conducting evidentiary hearings in each case, and conducting a joint hearing in which expert testimony was taken and made applicable to all twenty-three cases, three district court judges held that all arbitration provisions in all account agreements at issue in all twenty-three lawsuits were unenforceable.

Piper Jaffray appealed all decisions to the Montana Supreme Court except one which settled. Of the twenty-three cases, thirteen have settled, six were denied certiorari by this Court, two recently have been decided by the Montana Supreme Court (including the one at issue here), one was remanded to the Trial Court for further findings, and one is still pending appeal in the Montana Supreme Court. (App. 76).

The first decision of the Montana Supreme Court was in *Willems v. U.S. Bancorp Piper Jaffray Inc., et al.*, 2005

MT 37, 107 P.3d 465 (decided February 22, 2005). (App. 37-49).[7] The Montana Supreme Court later entered its decision in the case at issue here and incorporated its analysis in *Willems* as the basis for its decision. (App. 1-5).

In *Willems*, the Montana Supreme Court held a provision in the Non-IRA Agreements created a fiduciary duty owed by Piper Jaffray to its customers to just explain the arbitration provision, and no other contract provision, *before* the customer executed the account agreement. *Id.* at ¶¶ 24-28 (App. 47-48). The Court found Piper Jaffray breached that duty. *Id.* at ¶ 28 (App. 48).

The Non-IRA Account Agreements contain a margin agreement permitting customers to purchase securities with funds loaned from Piper Jaffray, so long as the customers maintain a certain balance in their accounts. The provision contained in the Non-IRA Agreements the Court found created the fiduciary duty, even before the agreement was signed, pertains to Piper Jaffray's rights to protect itself upon the death or incapacity of the customer in case the customers' securities decline in value and Piper Jaffray is at risk of not being repaid the funds it loaned the customer. The provision is as follows:

> **Customer's Orders Binding Until Notice of Death**
>
> Upon your death or failure to comply with any part of this Agreement or whenever Piper Jaffray deems it necessary for its protection, Piper Jaffray is authorized (but is not required) to:
>
> – Cancel outstanding orders;
>
> – Purchase, sell, assign, receive and deliver all or any part of the securities held or carried for you; and

[7] *Willems* settled shortly before the Montana Supreme Court issued its opinion and before the parties had moved to dismiss the appeal as moot. As a result, *Willems* is not one of the cases for which review by this Court can be sought.

> – Close out short sales by purchase upon any exchanged board or market any public or private sale at Piper Jaffray's option.

Willems at ¶ 17 (App. 43-44).

This provision is only contained in the Non-IRA Agreements, and is *not* in the IRA Agreements. The Montana Court nonetheless held this provision created a fiduciary duty of the broker to explain arbitration in the IRA Agreements. The Court rejected Piper Jaffray's arguments that this provision is not effective until the agreement is signed, that the provision does not grant Piper Jaffray unfettered discretion in the account, but only grants limited discretion to Piper Jaffray *after* the agreement is executed and upon death or incapacity of the customer, that Piper Jaffray must include this language to comply with federal regulations concerning margin accounts, and that an unfettered grant of discretion cannot derive from the middle of a provision concerning Piper's rights upon death. *Willems* at ¶¶ 17-28 (App. 43-48).

REASONS FOR GRANTING THE WRIT

Introduction

Since 1994, when the Montana Supreme Court rendered its first opinion in *Casarotto v. Lombardi*, 268 Mont. 369, 886 P.2d 931 (1994) ("*Casarotto I*"), the Montana judiciary has evidenced a hostility toward arbitration and has rejected arguments that the Federal Arbitration Act preempts the attempts of both the Montana legislature and judiciary to void pre-dispute arbitration agreements in matters clearly involving interstate commerce.

In *Casaratto I*, a Montana statute required any contract containing an arbitration provision to place a notice of the arbitration provision on the first page of the contract otherwise the arbitration provision was invalid and unenforceable. The Montana Supreme Court held this requirement did not violate the Federal Arbitration Act. *Casarotto I*, 268 Mont. at 382, 886 P.2d at 939. Justice Trieweiler's specially concurring opinion provides compelling insight

into the Montana Supreme Court's hostility toward the Federal Arbitration Act and well-settled law favoring arbitration as a means of dispute resolution: "I am particularly offended by the attitude of federal judges [who favor arbitration as an alternative dispute resolution mechanism which relieves crowded court dockets]. . . . [I]f the Federal Arbitration Act is to be interpreted as broadly as some of the decisions of our federal courts would suggest, then it presents a serious issue regarding separation of powers." *Casarotto I*, 286 Mont. at 382-385, 886 P.2d at 939-41.

This Court granted certiorari, *decided sub nom Doctor's Associates v. Casarotto,* 515 U.S. 1129 (1995) ("*Doctor's Associates I*"), and ordered the judgment of the Montana Supreme Court be vacated and remanded for further consideration in light of this Court's then-recent decision, *Allied-Bruce Terminix Cos. v. Dobson,* 513 U.S. 265 (1995).

Upon remand, the Montana Supreme Court affirmed its prior decision. *Casarotto v. Lombardi*, 274 Mont. 3, 901 P.2d 596 (1995) ("*Casarotto II*"). This Court again granted certiorari and reversed the decision of the Montana Supreme Court, *decided sub nom Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681 (1996) ("*Doctor's Associates II*"), holding the statute applicable to arbitration clauses violated the Federal Arbitration Act.

The Montana Supreme Court's hostility toward the Federal Arbitration Act and arbitration has not abated since *Casarotto I* and *II*. *See, e.g., Keystone, Inc. v. Triad Systems Corp.*, 1998 MT 326, 292 Mont. 229, 971 P.2d 1240 (1998) (invalidating portion of arbitration clause that required parties to arbitrate disputes outside of Montana); *Iwen v. U.S. West Direct*, 293 Mont. 512, 977 P.2d 989 (1999) (striking arbitration provision in advertising contract as "unconscionable"); *Kingston v. Ameritrade, Inc.*, 302 Mont. 90, 12 P.3d 929 (2000) (validity of arbitration provision in an agreement to be decided by court where validity of underlying agreement not at issue); *Kloss v. Edward D. Jones*, 2002 MT 129, 54 P.3d 1 (2002),

cert. denied, 538 U.S. 956 (2003) (arbitration provision not within the client's reasonable expectation and existence of an on-going fiduciary relationship required explanation of arbitration provision).

The Montana Supreme Court's decision at issue here continues this hostility towards arbitration by imposing a heightened duty on broker-dealers and brokers to explain arbitration provisions, but no other contract provisions, to the customer before the customer signs the agreement creating the duty, and wholey invalidating arbitration agreements in securities accounts. The Montana Supreme Court's decision, therefore, violates the Federal Arbitration Act and hinders the ability of broker-dealers to rely upon standardized contracts nationwide in violation of the Commerce Clause.

The Montana Supreme Court's imposed heightened duty to explain arbitration provisions to customers is in direct conflict with decisions of four other State Supreme Courts. *Dinsmore v. Piper Jaffray,* 593 N.W.2d 41 (S.D. 1999) (finding fiduciary duties are not owed when parties are dealing at arm's length; Piper Jaffray acts on its own behalf when negotiating and executing account agreements); *Rosenthal v. Great Western Financial Securities Corp.*, 926 P.2d 1061 (Cal. 1996) (finding fiduciary duties of a broker do not extend to orally alerting the customer to the existence of an arbitration clause or explaining its meaning and effect); *Jones v. Merrill Lynch, Pierce, Fenner & Smith*, 604 So.2d 332 (Ala. 1991) (finding absence of explanation by broker-dealer of arbitration agreement to customer does not constitute a breach of a fiduciary duty); *ABM Farms, Inc. v. Woods*, 692 N.E.2d 574 (Ohio 1998) (finding law did not require broker-dealer to explain arbitration provision, or any other aspect of contract to party prior to signing).

In fact, the U.S. Court of Appeals for the Seventh Circuit has squarely put the burden on the *investor* to inquire about the arbitration clause. *Pierson v. Dean, Witter, Reynolds, Inc.*, 742 F.2d 334 (7th Cir. 1984) (investors

cannot use their failure to inquire about the ramifications of the arbitration clause to avoid the consequences of agreed-to arbitration in claiming the clause is unconscionable).

Also, the Montana Supreme Court's wholesale invalidation of arbitration agreements approved by the U.S. Securities and Exchange Commission ("SEC") and used throughout the entire securities industry is contrary to decisions from at least three Federal Courts of Appeals and sixteen State Supreme Courts which routinely enforce these highly regulated arbitration provisions in securities account agreements. *See* section II, *infra*. Only the Supreme Judicial Court of Maine has taken a hostile view of arbitration provisions in securities agreements akin to the Montana decision. *Barrett v. McDonald Investments*, 870 A.2d 146 (Me. 2005). The Maine decision invalidated a predispute arbitration provision in a securities agreement and candidly explained that its decision was "a retreat from [its] previously broad presumption in favor of arbitration." *Id.* at 151. The concurring opinion elaborated by stating appellate courts are starting to distinguish and weaken U.S. Supreme Court precedent pertaining to arbitration. *Id.* at 152-53 (Alexander, J., concurring).

The Montana Supreme Court's improper imposition of unique and heightened standards for arbitration provisions and invalidation of arbitration provisions themselves in securities agreements disrupts the operations of the entire securities industry. National securities firms like Piper Jaffray routinely rely upon unilaterally drafted customer contracts containing SEC approved arbitration agreements. Based upon the Montana Supreme Court's decision at issue here, Montana-only account agreements and procedures would be required to be implemented by broker-dealers operating in a national securities market. Tailoring its agreements to comply with Montana' strict arbitration agreement standards could potentially force Piper Jaffray into non-compliance with national regulations concerning mandatory language in arbitration

provisions in securities agreements. The decision also questions the enforceability of arbitration provisions in securities agreements when a customer with an existing account agreement moves to Montana, or moves from Montana to another state.

Not only will the Montana decision adversely affect all broker-dealers doing business in Montana, but its impact will be felt far beyond the securities industry. This decision is not limited to Piper Jaffray, the securities industry or Montana. It will be used to invalidate arbitration provisions contained in any standardized contract routinely used nationwide by any business. In fact, the concurring opinion in *Barrett*, *supra*, after concluding appellate courts are eroding U.S. Supreme Court precedent relating to arbitration, cites a Ninth Circuit decision invalidating an arbitration provision in a franchise agreement, and a Second Circuit decision invalidating an arbitration provision in a reinsurance contract, in addition to *citing Willems*, the basis for the Montana decision at issue here. *Id.* at 152-53 (Alexander, J., concurring).

Moreover, a Florida Supreme Court decision invalidating an arbitration provision and distinguishing this Court's ruling in *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967) is currently pending before this Court. *Buckeye Check Cashing, Inc. v. Cardegna, et al.*, 894 So.2d 860 (2005), *cert. granted*, 74 U.S.L.W. 3272 (U.S. June 20, 2005) (No. 04-1264). In *Prima Paint*, this Court held the Federal Arbitration Act does not permit a party to avoid enforcement of an arbitration agreement by claiming the underlying contract, but not the arbitration agreement contained in the contract, was fraudulently induced. *Prima Paint* at 406. In *Buckeye*, the Florida Supreme Court distinguished *Prima Paint* by concluding the contract in *Prima Paint* was *voidable*, whereas the contract in Buckeye was *void*. *Buckeye* at 863. This Court granted certiorari in *Buckeye* on June 20, 2005, and recently heard oral arguments on November 29, 2005.

The Florida Supreme Court in *Buckeye* focused on the validity of the underlying contract as grounds to avoid enforcement of the arbitration agreement. Unlike *Buckeye*, the Montana Supreme Court here focused solely on invalidating the arbitration agreement by creating special rules for arbitration agreements only, while apparently conceding the validity of other contract terms. In fact, the Montana Supreme Court made it effortless for any investor to attack the arbitration agreement and avoid enforcement of the arbitration agreement by creating standards that only apply to arbitration provisions so strict and so unique, that no broker-dealer could possibly comply with them. No state, including Montana, can apply special standards to arbitration in violation of *Doctor's Associates II* in order to make it easier for customers to attack arbitration clauses and thus avoid enforcement of arbitration agreements in compliance with *Prima Paint*.

Addressing the Montana Supreme Court decision here along with *Buckeye* will allow this Court to comprehensively and uniformly address enforcement of arbitration agreements contained in standardized agreements used across the entire United States and to reinforce this Court's precedent pertaining to arbitration, both in situations where the underlying contract as a whole is attacked and where the attack is leveled solely against the arbitration clause. Absent this Court's intervention, Montana will continue to improperly apply special heightened standards to arbitration causing disruption throughout the securities industry and creating a basis for other courts to erode this Court's previous rulings favoring arbitration agreements in the highly regulated securities industry.

I. The Montana Supreme Court's unique judicially imposed requirement that pre-dispute arbitration clauses commonly contained in securities industry customer agreements must be explained to the customer before the agreement is even executed, which requirement is not applied to any other contract provisions in Montana and in direct conflict with decisions of four State Supreme Courts and five Federal District Courts, violates the Federal Arbitration Act and frustrates the national policy of favoring arbitration as a means of dispute resolution.

It is well established that a national policy favoring arbitration is at the heart of the Federal Arbitration Act. *Southland Corp. v. Keating*, 465 U.S. 1, 10 (1984); *see also First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 945 (1995); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 631 (1985). The *Southland* Court, in reversing the California Supreme Court, determined that section 2 of the Federal Arbitration Act applies to state court decisions and preempts conflicting state laws. *Southland, supra*, at 16. And, in *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987), this Court held that national policy applicable to securities industry claims, stating:

> [W]e are well past the time when judicial suspicion of the desirability of arbitration and of the competence of arbitral tribunals should inhibit enforcement of the Act in controversies based on statutes.

Id. at 226 (citations omitted).[8]

---

[8] Prior Montana law also provides a state policy favoring arbitration. *Chor v. Piper, Jaffray & Hopwood, Inc.*, 261 Mont. 143, 148, 862 P.2d 26, 29 (1993); *Vukasin v. D.A. Davidson & Co.*, 241 Mont. 126, 133, 785 P.2d 713, 718 (1990).

The national policy in favor of arbitration preempts state laws that infringe upon the domain Congress encompassed within the Federal Arbitration Act. For example, in *Perry v. Thomas*, 482 U.S. 483 (1987), this Court held that section 2 of the Federal Arbitration Act preempted a provision of the California Labor Code that permitted court actions to collect wages, notwithstanding any private agreement to arbitrate such a dispute. In dicta, the *Perry* Court stated that a court may not "rely on the uniqueness of an agreement to arbitrate as a basis for a state-law holding that enforcement would be unconscionable, for this would enable the court to effect what we hold today the state legislature cannot." *Perry*, *supra*, at 492, n. 9.

In the instant case, the Montana Supreme Court has done precisely what this Court counseled against in *Perry* by holding pre-dispute arbitration provisions to higher or different standards than other provisions in the contracts. The Montana Court held a substantive provision contained in the Non-IRA Agreements created a fiduciary duty requiring Piper Jaffray to explain the arbitration provision, and no other contract provision, to its clients *prior* to execution of the contract and by extension, prior to there even being a broker-client relationship.[9] The Montana Supreme Court ignored the clear holding of *Doctor's Associates II*, *supra*, and the dicta in *Perry*, *supra*, by imposing a heightened legal standard to an arbitration provision, and not to any other contract provision. This violates the Federal Arbitration Act.

Section 2 of the Federal Arbitration Act "makes enforceable a written arbitration provision in 'a contract *evidencing* a transaction *involving* commerce.' 9 U.S.C. § 2." *Allied-Bruce*, *supra*, at 836 (emphasis in original). As this Court further explained, section 2 also allows states to

---

[9] The decision does not discuss how this explanation is to be provided or memorialized. Must the explanation be in writing? Must it be recorded? Does it require the client to sign a separate document acknowledging that the explanation had been provided?

"regulate contracts, including arbitration clauses, under general contract law principles and they may invalidate an arbitration clause 'upon such grounds as exist at law or in equity for the revocation of *any* contract.' 9 U.S.C. § 2 (emphasis added). What states may not do is decide that a contract is fair enough to enforce its basic terms (price, service, credit), but not fair enough to enforce its arbitration clause." *Id.* at 281.

In the case at bar, the Montana Supreme Court imposed a higher burden on arbitration provisions than any other contract provisions. To do so, it found the following language contained in the Non-IRA Agreements created a fiduciary duty:

> **Customer's Orders Binding Until Notice of Death**
>
> Upon your death or failure to comply with any part of this Agreement or whenever Piper Jaffray deems it necessary for its protection, Piper Jaffray is authorized (but is not required) to:
>
> – Cancel outstanding orders;
>
> – Purchase, sell, assign, receive and deliver all or any part of the securities held or carried for you; and
>
> – Close out short sales by purchase upon any exchanged board or market any public or private sale at Piper Jaffray's option.

Willems, *supra* ¶¶ 17-28 (App. 43-48). The Montana Supreme Court held this fiduciary duty includes an obligation of the broker to explain the arbitration provision to the customer *before* the customer signs the agreement which necessarily is before the establishment of a broker-client relationship. *Id.*

This position completely ignores the fact that the contracts at issue clearly and specifically advise the client of the existence of the arbitration provision. The arbitration notice is found above the signature block and provides that, by signing the agreement, the client acknowledges

the existence of the arbitration clause. The language on the signature page of each Account Agreement clearly and unambiguously informs the customer that the Account Agreements contain arbitration provisions and acknowledges receipt of the agreement. The notice provision is generally in all capital and bold lettering, and directs the signer to the location of the arbitration provision in the Account Agreement. Therefore, any customers who sign the signature page of any Account Agreement cannot do so without first seeing the arbitration notice provision which clearly refers to the arbitration clause. Also, the language used in both the arbitration clause and the notice provision has been approved by the Securities Exchange Commission ("SEC") and is consistent with the requirements imposed by both the NYSE and NASD which are themselves overseen by the SEC. Finally, although the Montana Supreme Court held language contained in the Non-IRA Agreements created the fiduciary duty, it held that duty applied to the IRA Agreements as well, even though the IRA Agreements do not contain the provision the court found created a fiduciary duty.

Notwithstanding this, the Montana Supreme Court, as its only basis for voiding the arbitration provision, held Piper Jaffray had a fiduciary duty to explain the arbitration provision to each customer *before* the customer signed the agreement. This conclusion stands contract law on its head and creates a special requirement applicable only to arbitration provisions.

Montana contract law acknowledges that a written contract is only effective at delivery – not prior to delivery and certainly not prior to execution. *See, generally.*, Mont. Code Ann. § 28-2-906. It also recognizes that a party to a contract is generally bound by all terms of the contract, regardless of which terms were read. *See, generally, Wiley v. Iverson*, 295 Mont. 511, 518, 985 P.2d 1176, 1181 (1999); *see also, Schlemmer v. North Central Life Co.*, 307 Mont. 203, 206-207, 37 P.3d 63, 65 (2001) (where language in an insurance application is clear and unambiguous, plaintiff did not deny signing it, and contract has notation directly

above signature block attesting to signatory's understanding of the document, plaintiff's professed claim of ignorance as to the application's contents "cannot prevail.") Furthermore, Montana law provides there is no fiduciary duty between an investment advisor and his or her client absent a grant of discretionary authority. *See Chor v. Piper Jaffray*, 261 Mont. 143, 153, 862 P.2d 26, 32 (1993).

The Montana Court did not require Piper Jaffray to explain any other provision or condition in the Account Agreements before the Respondents executed them, including the provision the Court found created the fiduciary duty. The arbitration provision is thus impermissibly singled out and treated like no other provision. This requirement is as offensive and impermissible as the statutory requirement stricken in *Doctor's Associates II*, *supra*, that notice of the existence of the arbitration provision be provided on the first page of the agreement.

The Montana Supreme Court's imposed heightened duty to explain arbitration provisions to customers is in direct conflict with decisions of four other State Supreme Courts, one involving Piper Jaffray. In *Dinsmore v. Piper Jaffray*, 593 N.W.2d 41 (S.D. 1999), an investor brought an action against Piper Jaffray and its broker alleging the broker engaged in improper trading practices. *Id.* at 43. Piper Jaffray moved to compel arbitration based upon arbitration provisions contained in the account agreements for the accounts of which the investor complained. The trial court denied Piper Jaffray's motion holding Piper Jaffray had a fiduciary duty to explain the arbitration provisions to the investor and that Piper Jaffray breached that duty which allowed the investor to avoid enforcement of the arbitration agreement. *Id.* at 45. Piper Jaffray appealed. After examining the Federal Arbitration Act, this Court's decision in *Allied-Bruce Terminix Cos., v. Dobson*, 513 U.S. 265 (1995), and pertinent state law, the Supreme Court of South Dakota reversed the trial court's decision and held Piper Jaffray did not have a fiduciary duty to explain the arbitration agreement because the

parties were dealing at arm's length when they were negotiating and executing the agreements. *Id.* at 47. The Court explained:

> By the actual process of negotiating and executing these contracts Piper does not manage [the investor's] property nor does it act for or on behalf of [the investor]. Piper acts on its own behalf.

Id.

Similarly, in *Rosenthal v. Great Western Financial Securities Corp.*, 926 P.2d 1061 (Cal. 1996), investors brought an action against a broker-dealer and its broker alleging various tort claims. *Id.* at 1061. The broker-dealer filed a motion to compel arbitration based upon arbitration provisions contained in the account agreements at issue. *Id.* at 1061. The trial court denied the motion and the broker-dealer appealed. *Id.* at 1061. On appeal, the investors argued the broker-dealer had a fiduciary duty to explain the arbitration provision and the broker-dealer breached that duty, therefore, the investors could avoid enforcement of the arbitration agreement. *Id.* at 1080. After considering the Federal Arbitration Act, the California Supreme Court reversed the denial of the motion to compel arbitration and found the broker-dealer did not have a fiduciary duty to explain the arbitration provision. The Court stated:

> At the times the claimed nondisclosures occurred, no agency relationship had yet been formed, and those aspects of a broker's duty that derive from his or her role as the investor's agent are therefore not applicable. Under these circumstances, we find no authority for the proposition the fiduciary obligations of a broker extend to orally alerting the customer to the existence of an arbitration clause or explaining its meaning and effect.

Id.

The Alabama Supreme Court and Ohio Supreme Court also agree that a broker does not have a duty to explain an arbitration clause to a customer. *Jones v.*

Merrill Lynch, Pierce, Fenner & Smith, 604 So.2d 332 (Ala. 1991) (finding absence of explanation by broker-dealer of arbitration agreement to customer does not constitute a breach of a fiduciary duty); *ABM Farms, Inc. v. Woods*, 692 N.E.2d 574 (Ohio 1998) (finding law did not require broker-dealer to explain arbitration provision, or any other aspect of contract to party prior to signing).

The Montana Supreme Court's imposed fiduciary duty requirement is also contrary to decisions of five Federal District Courts. *Gouger v. Bear, Stearns & Co., Inc.*, 823 F.Supp. 282 (E.D.Pa. 1993) (finding a broker's duty does not require an explanation to the customer of the arbitration agreement); *Bender v. Smith Barney, Harris Upham & Co. Inc.*, 789 F.Supp. 155 (D.N.J. 1992) (extending law that brokers are not required as a matter of law to disclose or explain arbitration clauses to the customer to find broker-dealer had no duty to disclose arbitration clause to broker in Form U-4 agreement); *Curtis v. Newhard, Cook & Co., Inc.*, 725 F.Supp. 1072 (E.D. Mo. 1989) (finding brokers are not required as a matter of law to disclose or explain arbitration clauses to the customer); *Benoay v. E.F. Hutton & Co. Inc.*, 699 F.Supp. 1523 (S.D. Fla. 1988) (finding customer could not avoid arbitration by claiming arbitration clause was not explained to her); *Rush v. Oppenheimer & Co. Inc.*, 681 F.Supp. 1045 (S.D.N.Y. 1988) (holding brokers are not required as a matter of law to disclose or explain arbitration clauses to the customer).

Further, the U.S. Court of Appeals for the Seventh Circuit while not addressing the broker's duty, found the investor cannot avoid arbitration if the investor failed to inquire or chose not to inquire about the arbitration clause. *Pierson v. Dean, Witter, Reynolds, Inc.*, 742 F.2d 334 (7th Cir. 1984) (customers cannot use their failure to inquire about the ramifications of the arbitration clause to avoid the consequences of agreed-to arbitration in claiming the clause is unconscionable). Moreover, the Supreme Courts of Texas and California found the arbitration agreement itself adequately explained arbitration to the

investor. *In re McKinney*, 167 S.W.3d 833 (Tex. 2005); *see also, Rosenthal* at 1080, *supra*. (arbitration agreement includes an explanation of meaning of arbitration, that arbitration is final and binding, that parties to arbitration waive their right to jury trial, and that judicial review of the award is "strictly limited.")

In addition, the provision the Montana Supreme Court found created this fiduciary duty fulfills Piper Jaffray's regulatory obligations to liquidate margin accounts in certain circumstances, and is found in virtually every margin account agreement in the securities industry. The absence of this language in a margin agreement would call into question Piper Jaffray's ability to comply with federal regulations. Piper Jaffray, even with the language held to create discretion and thus a fiduciary duty, did not have unfettered discretion to buy and sell securities in Respondents' accounts because it could only act in limited situations and only within the bounds of the common law. Piper Jaffray's "discretion" was constrained in two ways: (1) Piper Jaffray could only decide to act in three discrete situations; and, (2) when it did act, Piper Jaffray was constrained by an implicit requirement that it do so in good faith and in a commercially reasonable manner. Accordingly, the Montana Supreme Court's finding that "Piper's brokers [had] discretion to buy and sell securities" hinders Piper Jaffray's ability to comply with federal regulations in non-discretionary accounts, such as the ones here.

In the context of a margin account, like those at issue in this case, the language the Montana Supreme Court relied upon to find a fiduciary duty, merely provides protection to Piper Jaffray in the event of death, incapacity or adverse market conditions.[10] Piper Jaffray is allowed

[10] If a customer's account decreases below a certain percentage of the customer's margin loan, Piper Jaffray's ability to be repaid the loaned funds may be at risk. This threatens Piper Jaffray's capital which if impaired would harm all of its customers. Piper Jaffray is, therefore, entitled to either require the customer to add money to the

(Continued on following page)

to act in only three very specific situations: (1) when the customer dies; (2) when the customer breaches the contract; or, (3) when Piper Jaffray deems it necessary to liquidate the account for its protection. *See Willems, supra*, ¶ 17 (App. 43). It is the third situation the Court below relied upon to find Piper Jaffray had a fiduciary duty to explain the arbitration provision.

The purpose of such language, however, "is to protect brokers from the risks associated with insufficiently secured accounts, and to prevent customers from carrying vast exposure in their accounts without adequate capital to cover their positions." *Pomano-Windy City Partners, Ltd. v. Bear Stearns & Co., Inc.*, 794 F.Supp. 1265, 1275 (S.D.N.Y. 1992) (citations omitted). As Justice Powell stated, sitting by designation on the Fourth Circuit and interpreting similar language, "A brokerage house should not have to risk a nearly unlimited amount of its own funds while waiting [for a client to] meet a margin call." *Prudential-Bache Securities, Inc. v. Stricklin*, 890 F.2d 704, 707 (4th Cir. 1989).[11]

---

account through a margin call, or to buy or sell in the account to eliminate or decrease the risk (*i.e.* to liquidate the account).

[11] The language in that contract was very similar to the language in the Piper Jaffray contracts at issue in this matter and read:

> Whenever in your [appellee's] discretion you deem it desirable for your protection (and without the necessity of a margin call) . . . you may, without prior demand, tender, and without any notice of the time or place of sale, all of which are expressly waived, . . . buy any securities, or commodities or contracts relating thereto of which my account or accounts may be short, in order to close out in whole or in part any commitment in my behalf . . . and neither any demands, calls, tenders or notices which you may make or give in any one or more instances nor any prior course of conduct or dealings between us shall invalidate the aforesaid waivers on my part.

Prudential-Bache, 890 F.2d at 706.

The brokerage firm's discretion to increase the margin or to initiate a margin call "must be exercised in good faith." *Modern Settings, Inc. v. Prudential-Bache Securities, Inc.*, 936 F.2d 640, 644 (2nd Cir. 1991). "A margin call is made in bad faith when it is 'contrived . . . in bad faith to penalize [the customer] for some reason unrelated to [the broker's] business." *Capital Options Investments, Inc. v. Goldberg Brothers Commodities, Inc.*, No. 88 C 2073, 1990 WL 180583, *5 (N.D. Ill. Nov. 5, 1990) (citations omitted) (alterations in original). Accordingly, and in contradiction to the Montana Supreme Court, Piper Jaffray did not have absolute discretion to initiate a margin call or to liquidate the account upon a determination that it was in its best interests to do so. *See Modern Settings*, 936 F.2d at 644 (holding that a brokerage did not have "absolute discretion" to liquidate because it must make this decision in good faith).

Similarly, Piper Jaffray, after determining that liquidation of the account was necessary, would also be constrained to do so "in good faith and in a commercially reasonable manner." *In re Kaplan*, 143 F.3d 807, 818 (3rd Cir. 1998). Liquidating in a commercially reasonable manner means to mitigate the damages of the client. *See Agra, Gill & Duffus, Inc. v. Benson*, 920 F.2d 1173, 1177 (4th Cir. 1990) ("overriding the broker's discretion to select the manner of liquidation was its duty to mitigate [the client's] damages, which in this context meant to liquidate in a commercially reasonable manner."). *See also Cauble v. Mabon Nugent & Co.*, 594 F.Supp. 985, 992 (S.D.N.Y. 1984) (in commodities case, holding that "broker does not have unbridled discretion to liquidate an account; its power to liquidate must be exercised in good faith under the existing facts and circumstances").

Because Piper Jaffray's actions were constrained by the duty to act (1) in good faith, and, (2) in a commercially reasonable manner in deciding when and how to liquidate the accounts, Piper Jaffray did not have discretion over the Respondents' accounts. Therefore, the holding that

Piper Jaffray somehow owed the Respondents a fiduciary duty lacks any support.

The inescapable conclusion is that the Montana Supreme Court, in its hostility to arbitration, has seized upon a unique interpretation of principles of contract law to void the arbitration clauses, and only the arbitration clauses, in the plaintiffs' contracts. Arbitration in Montana is not only disfavored, but barred from use by the securities industry based upon a unique and result-oriented judicial interpretation of principles of contract law to find the arbitration clause unenforceable. A Writ of Certiorari should be issued here expressly because these decisions are directly contrary to this Court's precedent.

II. The Montana Supreme Court's wholesale invalidation of pre-dispute arbitration clauses common in the securities industry is in step with the Supreme Judicial Court of Maine but out of step with at least three U.S. Courts of Appeal and sixteen State Supreme Courts which routinely enforce arbitration clauses contained within customer agreements in the securities industry.

It is beyond dispute that the securities industry generally, and the relationship between broker-dealers and their customers in particular, are matters in interstate commerce, 15 U.S.C. § 78(b)(1), and thus come within the Federal Arbitration Act. In this instance, the decisions of the Montana Supreme Court at issue here interfere with the arrangement between broker-dealers located in other states and their Montana customers who are investors in national securities markets. Firms like Piper Jaffray, operating as broker-dealers in the heavily regulated securities industry, routinely rely upon unilaterally drafted customer contracts. In fact, the SEC requires firms

to use certain language in its arbitration provisions, which language is set forth in Rule 3110 of the NASD Manual. These contracts are executed by broker-dealers and their customers throughout the country.

There is a reasonable expectation that arbitration clauses are found in agreements between broker-dealers and their clients. Indeed, prior to these Montana decisions, this expectation has been part of Montana contract law and has been discussed in connection with arbitration clauses in brokerage agreements. *See, Passage v. Prudential-Bache Securities Inc.*, 223 Mont. 60, 66, 727 P.2d 1298, 1302 (1986) ("Such predispute arbitration agreements are not outside the reasonable expectations of the investor." (*citing, Finkle and Ross v. A.G. Becker Paribas, Inc.*, 622 F.Supp. 1505, 1511-12 (S.D.N.Y 1985)).

The prevalence and the use of arbitration in the securities industry is evidenced by recent statistics published by the NASD. In the last five years alone the NASD has administered over 33,000 arbitrations. During that time, of those claims decided by NASD arbitration panels, approximately 55% resulted in awards in favor of the investor. In 2004 alone, the NASD administered over 9,000 arbitrations.

Not only are pre-dispute arbitration provisions usually and customarily employed in the securities industry, but their use has been acknowledged and accepted by this Court as a legitimate and fundamentally fair means of resolving disputes between broker-dealers and their customers. *Shearson/American Express, Inc.*, 482 U.S. at 237. In fact, Montana law prior to the *Casarotto I* and *II* decisions, held that "agreement[s] to arbitrate disputes in accordance with SEC-approved procedures are not unconscionable as a matter of law." *Chor v. Piper, Jaffray & Hopwood, Inc.*, 261 Mont. 143, 149-150, 962 P.2d 26, 30 (1993) (*citing Cohen v. Wedbush, Noble, Cooke, Inc.*, 841 F.2d 282, 286 (9th Cir. 1988) (overturned on other grounds)).

Indeed, several U.S. Courts of Appeal recognize the enforceability of pre-dispute arbitration provisions in contracts between broker-dealers and their clients. *See, e.g., Threlkeld v. Metallgesellschaft Ltd.*, 923 F.2d 245 (2nd Cir. 1991) (agreements between American investor and British metal futures trader would not be stricken as contracts of adhesion, so as to release investor from obligation to arbitrate dispute); *Securities Industry Ass'n v. Connolly*, 883 F.2d 1114 (1st Cir. 1989) (Federal Arbitration Act preempted Massachusetts from adopting regulations requiring arbitration clauses in pre-dispute arbitration agreements between broker-dealers and their customers to be conspicuous and to be subject to full written disclosure concerning their legal effect); *Pierson v. Dean, Witter Reynolds, Inc.*, 742 F.2d 334 (7th Cir. 1984) (found arbitration provision in contract between customer and investment brokerage firm would not be held unconscionable absent evidence beyond mere allegations of unfairness).

At least sixteen State Supreme Courts also regularly enforce pre-dispute arbitration provisions in securities contracts.[12]

---

[12] *Investment Management & Research, Inc. v. Hamilton*, 727 So.2d 71, 78 (Ala. 1999) ("Because Hamilton claimed fraud in the inducement of the customer-agreement contract generally, as opposed to the arbitration clause specifically, Hamilton's claims against IMR are subject to arbitration according to the terms of the customer agreement he signed."); *Jones v. Merrill Lynch, Pierce, Fenner & Smith*, 604 So.2d 332 (Ala. 1991) (finding absence of explanation by broker-dealer of arbitration agreement to customer does not constitute a breach of a fiduciary duty); *American Ins. Co. v. Cazort*, 871 S.W.2d 575 (Ark. 1994) (holding that the issuer could compel the investor into arbitration even though the issuer was not a signatory to the arbitration agreement between the investor and the broker); *Rosenthal v. Great Western Financial Securities Corp.*, 926 P.2d 1061 (Cal. 1996) (finding fiduciary duties of a broker do not extend to orally alerting the customer to the existence of an arbitration clause or explaining its meaning and effect); *ABM Farms, Inc. v. Woods*, 692 N.E.2d 574 (Ohio 1998) (finding law did not require broker-dealer to explain arbitration provision, or any other

(Continued on following page)

aspect of contract to party prior to signing); *Oppenheimer & Co., Inc. v. Young*, 475 So.2d 221 (Fla. 1985) (approving broker's right to arbitration of dispute pursuant to arbitration clause despite claims by investors even though broker did not pointlessly invoke the arbitration agreement in a prior federal court action); *Fairview Cemetery Assoc. v. Eckberg*, 385 N.W.2d 812, 821 (Minn. 1986) (Held that the investors "Minnesota Blue Sky Law and related common law claims are therefore subject to arbitration."); *Smith Barney, Inc. v. Henry*, 775 So.2d 722, 727 (Miss. 2001) ("Further, the arbitration provisions survive the death of Hilliard and the termination of the agreements and bind Henry as a successor of Hilliard."); *State ex. rel. PaineWebber, Inc., v. Voorhees*, 891 S.W.2d 126, 130 (Mo. 1995) ("Arbitration Act requires a court to stay a lawsuit pending arbitration where as here the parties agree in writing to arbitrate a dispute from a contract that involves commerce."); *Dowd v. First Omaha Securities Corp.*, 495 N.W.2d 36 (Neb. 1993); (Requiring arbitration of dispute, despite plaintiff's challenge of the impartiality of the arbitration panel); *Financial Network Investment Corp. v. Becker*, 741 N.Y.S.2d 837, 838 (N.Y. Sup. 2002) ("When valid arbitration agreement covering the dispute is shown, arbitration is required"); *David v. Merrill Lynch, Pierce, Fenner and Smith, Inc.*, 440 N.W.2d 269, 275 (N.D. 1989) ("We conclude that the arbitration agreement is applicable to David's claims against Williams and Merrill Lynch Commodities, Inc."); *Dean Witter Reynolds, Inc. v. Shear*, 796 P.2d 296, 302 (Okla. 1990) (concurring opinion) ("[P]arties to a commodities contract (should) be allowed to *knowingly* and *intentionally* waive the right to trial by jury by agreeing to submit contractual controversies to arbitration.") (emphasis in original); *Dickler v. Shearson Lehman Hutton, Inc.*, 596 A.2d 860, 867 (Pa. Super. Ct. 1991) ("Given the three paths down which this litigation can be directed – compelled individual arbitration, class action in a court of law, or compelled classwide arbitration – the last choice best serves the dual interest of respecting and advancing contractually agreed upon arbitration agreements while allowing individuals who believe they have been wronged to have an economically feasible route to get injunctive relief from large institutions employing adhesion contracts."); *Carlsten v. Oscar Gruss & Son, Inc.*, 853 A.2d 1191, 1194 (R.I. 2004) ("[P]arties who voluntarily contract to use arbitration as an expeditious and informal means of private dispute resolution are bound by the terms of their agreement."); *Dinsmore v. Piper Jaffray*, 593 N.W.2d 41 (S.D. 1999) (finding fiduciary duties are not owed when parties are dealing at arm's length; Piper Jaffray acts on its own behalf when negotiating and executing account agreements); *Cantella & Co., Inc. v. Goodwin*, 924 S.W.2d 943, 944 (Tex. 1996) ("Once a party seeking to compel arbitration establishes that an

(Continued on following page)

The Supreme Judicial Court of Maine, however, has recently taken a position similar to that of the Montana Supreme Court in contravention of these pro arbitration decisions. In *Barrett v. McDonald Investments*, 870 A.2d 146 (Me. 2005), the Maine Court in a "retreat from [its] previously broad presumption in favor of arbitration," invalidated an arbitration clause in an agreement between a broker-dealer and a customer because it found the arbitration clause ambiguous as to whether it pertained to the broker giving advice. *Id.* at 151. The concurring opinion expanded on the Court's rationale and even cited the Montana Supreme Court's decision at issue here in support of its retreat:

> The passage of time and events, particularly the increased use of contracts of adhesion containing mandatory arbitration clauses to avoid judicial enforcement of federal and state anti-discrimination and consumer protection laws, is leading many appellate courts to distinguish and weaken the significance of these [U.S. Supreme Court] precedents from an earlier time in the development of arbitration law . . . *Willems v. U.S. Bancorp Piper Jaffray, Inc.*, 2005 MT 37, ¶¶ 1, 27-28, 326 Mont. 103, 107 P.3d 465, 470. . . .

Id. at 153 (Alexander, J., concurring).

In summary, granting the Writ of Certiorari is appropriate here because the decision below is out of step with several U.S. Courts of Appeal and numerous State Supreme Courts which enforce pre-dispute arbitration provisions in the securities industry. This is of national

---

agreement exists under the FAA, and that the claims raised are within the agreement's scope, the trial court 'has no discretion but to compel arbitration and stay its proceedings pending arbitration.'"); *Garmo v. Dean, Witter, Reynolds, Inc.*, 681 P.2d 253, 255 (Wash. 1984) ("We hold that the supremacy clause of the federal constitution prevails and, thus, the federal arbitration law requires enforcement of arbitration clauses in brokerage agreements.")

importance because the Montana decisions will disrupt the whole securities industry because Montana-only account agreements and procedures would be required to be implemented by broker-dealers. Furthermore, if other states use Montana's decision as support to retreat from enforcing arbitration agreements and place special requirements on arbitration, like the Supreme Judicial Court of Maine, broker-dealers will have to tailor their agreements for each one of those states, further burdening the securities industry nationwide.

III. The Montana Supreme Court's wholesale invalidation of pre-dispute arbitration provisions common in the securities industry impermissibly interferes with the relationship between broker-dealers and their customers in interstate commerce and thus violates the Commerce Clause.

The United States Constitution gives Congress alone the power "[t]o regulate Commerce with foreign Nations, and among the several States. . . . " U.S. Const. art. I, § 8, cl. 3. Under this clause, Congress "is empowered to regulate and protect the instrumentalities of interstate commerce, or persons or things in interstate commerce, even though the threat may come only from intrastate activities." *Pierce County, Wash. v. Guillen*, 537 U.S. 129, 147 (2003), *citing*, *United States v. Lopez*, 514 U.S. 549, 558 (1995) (citations omitted).

Even in areas where Congress has not exercised this authority, state regulations may violate the Commerce Clause either because the regulations discriminate against interstate or foreign commerce, or because they incidentally affect such commerce. *Camps Newfound/Owatonna, Inc. v. Town of Harrison, Maine, et al.*, 520 U.S. 564 (1997). Discrimination against interstate commerce can be evident either on a statute's face, or in its practical effect. *See e.g., Wyoming v. Oklahoma*, 502 U.S. 437, 456 (1992). As explained by this Court over fifty years ago:

> Our system, fostered by the Commerce Clause, is that every farmer and every craftsman shall be encouraged to produce by the certainty that he will have free access to every market in the Nation, that no home embargoes will withhold his export, and no foreign state will by customs duties or regulations exclude them. Likewise, every consumer may look to the free competition from every producing area in the Nation to protect him from exploitation by any. Such was the intent of the Founders; such has been the doctrine of this Court which has given it reality.

H.P. Hood & Sons, Inc. v. Du Mond, 336 U.S. 525, 539 (1949).

Here, the practical effect of the Montana Court's decision is to create a situation whereby firms, such as Piper Jaffray, which conduct business in interstate commerce and routinely utilize unilaterally drafted contracts whose terms are influenced and governed by federal statutes and regulations and whose arbitration provisions are approved by the SEC and the Self-Regulatory Organizations, such as the NYSE and the NASD, overseen by and under the jurisdiction of the SEC, will not be able to rely upon such contracts if executed in Montana by Montana clients.

The decision also calls into doubt the enforceability of such provisions if a customer with an existing arbitration agreement moves to Montana, or moves from Montana to another state. This impairs free access to the state of Montana by Piper Jaffray as only customer contracts without arbitration clauses are seemingly permissible. This undue restriction on choice of dispute resolution and, indeed, the freedom to contract is in violation of the Federal Arbitration Act, and only serves to impair the contract rights of firms such as Piper Jaffray seeking to bring access to the various national securities markets and exchanges to Montana. The decisions below thus operate

an undue and substantial burden on interstate commerce and, in practical effect, violate the Commerce Clause.

The result of this unique propensity of the Montana judiciary to void arbitration agreements in Montana will hinder national broker-dealer firms' abilities to operate uniformly throughout the United States. This result offends the Commerce Clause by impeding interstate commerce and, as noted above, is out of step with numerous jurisdictions which recognize the enforceability of arbitration clauses in the securities industry.

CONCLUSION

For the foregoing reasons, Petitioners respectfully request that a Writ of Certiorari to the Montana Supreme Court be issued.

RESPECTFULLY submitted this 7th day of December 2005.

STANLEY T. KALECZYC
BROWNING, KALECZYC,
BERRY & HOVEN, P.C.
139 N. Last Chance Gulch
P.O. Box 1697
Helena, Montana 59624
(406) 443-6820
Counsel of Record

JOHN S. LUTZ
TAMARA A. HOFFBUHR
FAIRFIELD AND WOODS, P.C.
1700 Lincoln, Suite 2400
Denver, Colorado 80203
(303) 830-2400

120 P.3d 809, 2005 WL 1869393 (Mont.),

(The Court's decision is referenced in a "Decisions Without Published Opinions: table in the Pacific Reporter. See MT R S CT IOR 1 and MT R Opinion Forms & Cite STDS Opinion Forms and Citations.)

Supreme Court of Montana.
Raymond KAUFMAN, Individually and as Trustee of the Montana Facial Surgery Pension and Profit Plan and Janet L. Nothstine, Plaintiffs and Respondents,

v.

U.S. BANCORP PIPER JAFFRAY, INC. and Thomas J. O'Neill, and John Does I through X, Defendants and Appellants.
No. 04-491.

Submitted on Briefs Jan. 11, 2005.
Decided Aug. 9, 2005.

APPEAL FROM: District Court of the Second Judicial District, In and for the County of Silver Bow, Cause No. DV 2002-16, The Honorable Thomas M. McKittrick, Judge presiding.

For Appellant: Stanley Kaleczyc and Brand Boyar, Browning Kaleczyc Berry & Hoven, P.C., Helena, Montana; John S. Lutz, Fairfield & Woods, P.C., Denver, Colorado; Robert J. Phillips, Phillips & Bohyer, P.C., Missoula, Montana.

For Respondents: William P. Joyce, Joyce & Johnston, PLLP, Butte, Montana.

Justice PATRICIA O. COTTER delivered the Opinion of the Court.

¶ 1 Pursuant to Section I, Paragraph 3(c), Montana Supreme Court 1996 Internal Operating Rules, the following decision shall not be cited as precedent. It shall be filed as a public document with the Clerk of the Supreme Court and shall be reported by case title, Supreme Court cause number and result to the State Reporter Publishing Company and to West Group in the quarterly table of noncitable cases issued by this Court.

¶ 2 U.S. Bancorp Piper Jaffray, Inc., ("Piper") appeals an Order of the District Court for the Second Judicial District, Silver Bow County. Defendant Thomas J. O'Neill is a former Piper employee and is not a party to this appeal. The District Court denied Piper's motion to compel arbitration of claims filed against Piper by Raymond Kaufman ("Kaufman"), individually and as trustee of the Montana Facial Surgery Pension and Profit Sharing Plan ("Plan"), and Janet L. Nothstine ("Nothstine"). We affirm.

¶ 3 This case is one of twenty-three different lawsuits filed by investors of Piper involving the alleged mismanagement of the investors' accounts in Piper's branch office in Butte. The facts behind this particular action are that Nothstine opened a self-directed IRA on April 25, 1987, with Piper Jaffray and O'Neill. The account agreement establishing this IRA, which is the subject of this litigation, did not contain a provision regarding binding predispute arbitration. Nothstine later opened a separate Roth IRA, upon O'Neill's advice. At the time she did so, she was directed to sign a PAT Plus Account Agreement in order to create the Roth IRA. The PAT Plus document contained both a pre-dispute arbitration provision and a provision purporting to allow Piper to complete transactions within the client's account. Nothstine believed the two accounts were separate and distinct from each other.

However, after discovering alleged mismanagement within the original account and contacting an attorney, Nothstine learned that under the provisions of the PAT Plus account, Piper was insisting upon pre-dispute arbitration of disputes concerning her original and – to her mind – wholly separate IRA. It is undisputed that Nothstine signed the PAT Plus Account Agreement which created the Roth IRA in front of O'Neill. It would have been apparent to him that she did not read the arbitration clause before signing. He did not explain the ramifications of the arbitration clause to her.

¶ 4 Nothstine does not recall signing subsequent forms sent to her by Piper, but she apparently signed all documents provided to her, believing she needed to do so to maintain her accounts. The forms were presented to her on a take-it-or-leave-it basis. Nothstine was unaware of the significance of the arbitration provisions within the forms until she contacted an attorney to prosecute the claims underlying this litigation.

¶ 5 Kaufman is the trustee of and a participant in the Plan. He also maintained separate individual accounts with Piper. In 1998, Kaufman signed an agreement with Piper which opened the Plan's investment. At the time the events occurred which gave rise to this lawsuit, only Kaufman and Nothstine were participants in the Plan.

¶ 6 Kaufman is a busy physician with limited time to deal with his investment accounts. O'Neill was aware of the demands on Kaufman's time, and Kaufman relied on O'Neill to communicate details about his investment accounts as needed. When Kaufman was presented with documents dealing with his individual accounts, he did not believe that those accounts had anything to do with the

management of the Plan. No one at Piper explained that by opening additional accounts, Kaufman could affect the rights of the Plan and its participants. Kaufman signed a PAT Plus Account Agreement for the Plan after he received it in the mail with a letter stating that Piper was eliminating the type of account the Plan had previously had in place. The letter recommended the PAT Plus Account format, and explained that if Kaufman did not sign the new agreement, the Plan would be reassigned to a fee-paying account format. Kaufman signed the PAT Plus Account Agreement without reading it, and without being informed of its arbitration provisions. The agreement contained a pre-dispute arbitration provision and a provision purporting to allow Piper to complete transactions within the client's account whenever Piper "deems it necessary for its protection." Piper has demanded arbitration of the disputes in the Plan's accounts pursuant to the arbitration provisions contained in the PAT Plus document.

¶ 7 These facts and the issues arising from them are substantially identical to those presented in *Willems v. U.S. Bancorp Piper Jaffray, Inc.*, 2005 MT 37, ¶ 22, 326 Mont. 103, ¶ 22, 107 P.3d 465, ¶ 22, in which we held that a clause in a PAT Plus Account Agreement granting Piper broad discretion over an investor's holdings creates a fiduciary duty. That clause, in addition to an arbitration clause, was included in the pre-filled forms which Nothstine signed in connection with her Roth IRA account, and Kaufman signed when Piper informed him that the Plan's account format was being discontinued. *Willems* further held that in light of the fiduciary duty, Piper was obligated to advise investors of the consequences of the arbitration clause prior to the formation of the contract, and that

because Piper did not, the arbitration clause was unenforceable. *Willems*, ¶¶ 25, 28.

¶ 8 We have determined to decide this case pursuant to our Order dated February 11, 2003, amending Section 1.3 of our 1996 Internal Operating Rules and providing for memorandum opinions.

¶ 9 We conclude that, in light of *Willems*, this case is clearly controlled by settled Montana law. Therefore, we affirm the District Court's conclusion that Piper owed a fiduciary duty to explain the arbitration provision to Nothstine and Kaufman, that it breached that duty, and therefore, the pre-dispute arbitration provisions are unenforceable.

We Concur: BRIAN MORRIS, JAMES C. NELSON, W. WILLIAM LEAPHART and JOHN WARNER.

MONTANA SECOND JUDICIAL DISTRICT COURT,
SILVER BOW COUNTY

RAYMOND KAUFMAN, Individually and as Trustee of the MONTANA FACIAL SURGERY PENSION AND PROFIT PLAN and JANET L. NOTHSTINE Plaintiffs, vs. U.S. BANCORP PIPER JAFFRAY, INC., THOMAS J. O'NEILL, ROBERT ENGLISH AND JOHN DOES I through X, Defendants.	Cause No. DV-02-16 **FINDINGS OF FACT AND CONCLUSIONS OF LAW**

INTRODUCTION

Almost two dozen individuals who were investors with Piper Jaffray (Piper) at its Branch Office in Butte, Montana, have filed suits in the above-referenced cases against Piper as a result of its business practices and those of its account executive, Tom O'Neill. The lawsuits involve the investors' individual investment accounts which were created and maintained at the Butte office. While the circumstances surrounding the opening and maintenance of these accounts vary somewhat among those Plaintiffs, there is a similar fact pattern with respect to the essential facts surrounding the actual creation and maintenance of those accounts. Plaintiffs allege a number of common law tort claims which arise from a variety of illegal business

practices, such as "churning," unauthorized trading, and inappropriate trading. Plaintiffs allege that Piper failed to properly supervise O'Neill, who was at one time subject to a Consent Decree with the Montana State Auditor. The decree arose out of prior misconduct of O'Neill which had been uncovered following an administrative investigation in the 1990s. Piper had a duty to supervise O'Neill to insure that his misconduct and unethical practices as a broker would not be repeated. Plaintiffs allege that Piper not only allowed, but encouraged, O'Neill to repeat the proscribed business practices which had given rise to the Consent Decree.

Defendants have filed Motions to Compel Arbitration in all of the above-referenced cases. The motions gave rise to a series of hearings by the three Montana District Court Judges to whom these Piper cases have been assigned, Hon. Kurt Krueger, Hon. John W. Whelan, and Hon. Thomas M. McKittrick. Individual hearings took place with respect to many of the Plaintiffs who have a pending claim against Piper. Additionally, the three judges, sitting in an *en banc* configuration, heard the testimony, and received evidence, from "common expert witnesses" and "common fact witnesses." Those "common witness" hearings took place on August 12, 2003, and September 3, 2003, at which Plaintiffs called Professor William Corbett as a common expert witness. Plaintiffs called Jerry Campbell, a former Piper account executive, as a common fact witness. Defendants called Michael Perino, of New York, and Wendy Harmsen, of Minneapolis, as common expert and fact witnesses, respectively.

In a prior discovery deposition, Defendant Tom O'Neill refused to respond to questioning regarding the opening and formation of Plaintiffs' accounts, citing his Fifth

Amendment right against self-incrimination. Thus, there was no testimony presented by Defendants to refute the testimony of any Plaintiff with regard to the opening and maintenance of the account documents which they had signed which contained the pre-dispute arbitration clauses which are the basis of Defendants' motion to compel arbitration.

Following the conclusion of these common hearings, the parties submitted their post-hearing briefs on October 10, 2003. The Plaintiffs submit herewith their common proposed Findings of Fact and Conclusions of Law.

FINDINGS OF FACT

JANET NOTHSTINE

1. The Plaintiff, Janet Nothstine opened a self-directed IRA on April 25, 1997 with Piper Jaffray and Hopwood. The IRA account agreement did not contain a pre-dispute arbitration clause. (TR. Kaufman/ Nothstine, 7/24/2003, pg. 35)

2. As it relates to Janet Nothstine's IRA account, she has never signed a document which changed the relationship between herself and Piper. *Id.*

3. When Janet Nothstine signed the Roth IRA application (Exhibit E), she had a discussion with Tom O'Neill in which he stated that it was best for her not to close her regular IRA and to open a separate Roth IRA to put funds in from that point forward. Based upon that discussion Janet Nothstine thought that the two accounts were separate and distinct accounts. *Id.* at 36 and 37.

4. When Janet Nothstine signed the Roth IRA, O'Neill never advised that by opening the Roth IRA she

would in any way effect the regular IRA she had since 1987. *Id.*

5. When Janet opened the Roth IRA she was in Tom O'Neill's office and he gave her the papers to sign with the signature page open. Janet signed the application right away and it would have been apparent to O'Neill that she did not read the arbitration clause found within the body of the Agreement *Id.* at 38.

6. The current litigation concerning Janet Nothstine involves only the regular IRA account opened in 1987. *Id.* at 39.

7. As it relates to the PAT Plus agreements (Exhibits A and B), Ms. Nothstine reaffirmed in open court the truth of the statements she made in her affidavit filed with her Brief in Opposition to the Motion to Compel. *Id.* at 43.

8. Janet Nothstine does not recall receiving either the 1993 or the 1995 forms in the mail. She did not ask for these forms nor was she interested in changing her account or her relationship with Thomas O'Neill and Piper. She does not recall reading these forms and likely signed based upon the advice of either Mr. O'Neill or her husband. She likely signed the forms because she felt she needed to comply with Piper's request to maintain her accounts. See Affidavit at paragraph 6.

9. That as an unsophisticated investor, Janet Nothstine relied on O'Neill's representations about the purpose of the forms when signing all of the documents which were provided to her. Her discussions with O'Neill dealt only with her goals in maintaining the accounts and Mr. O'Neill advised that the documents she was signing were necessary for him to help her meet her goals. See Affidavit at paragraph 7.

10. Janet does not recall O'Neill ever explaining that in signing any of the forms which were provided for her signature that she was waiving her right to access the State Courts or that she was waiving her right to a jury trial. In fact, O'Neill never explained to Janet that if she had a dispute about how her account was being managed that she needed to pursue arbitration. See Affidavit at paragraph 8.

11. That the first time Janet was aware of the significance of the arbitration provisions was after she contacted an attorney to prosecute the claims of this litigation. Janet contacted and [sic] attorney after she was advised by the Montana Auditor's Office of serious security violations concerning her accounts. See Affidavit at paragraph 9.

12. That all of the documents Janet was asked to sign were prepared by Piper on pre-printed forms and were presented to her on a take-it-or-leave-it basis. Janet felt that she had no meaningful ability to negotiate the terms of any of the agreements. See Affidavit at paragraph 10.

13. Janet did not reasonably expect that by signing the forms she was allowing Piper to dictate where and how she could vindicate her rights should a problem arise with their handling of her accounts. See Affidavit at paragraph 11.

14. Beginning in 1993, Piper employed a form agreement which it called a PAT Plus Agreement to govern non-IRA accounts. The PAT Plus provided a credit feature and replaced Piper's PAT Agreement. (TR. Harsman, 9/13/03, at pg. 243).

15. The PAT Plus Agreement contains a pre-dispute arbitration provision which Piper seeks to enforce in this litigation.

16. All PAT Plus Agreements contain the following language under a section entitled "Securities Account":

> b. "Upon your death or failure to comply with any part of this Agreement *or whenever Piper Jaffray deems it necessary for its protection, Piper Jaffray is authorized (but is not required) to*:
>
> - Cancel outstanding orders;
> - Purchase, sell, assign, receive and deliver all or any part of the securities held or carried for you; and
> - Close out short sales by purchase upon any exchange board or market or any public or private sale at Piper Jaffray's option.
>
> (Emphasis added)

17. The PAT Plus agreements begin with the following language:

> This agreement ("Agreement") sets forth the terms and conditions governing the Piper Jaffray PAT Plus Account ("PAT Plus Account") offered by Piper Jaffray Inc. ("Piper Jaffray"), for which you (all such signatories hereto, whether acting in their individual or representative capacities, are sometimes referred to as "you") are making application with Piper Jaffray.

This language is inconsistent with the following language in the Pre-dispute Arbitration provision:

> You agree to arbitrate any disputes between Piper Jaffray and you. You specifically agree and recognize that all controversies which may arise between Piper Jaffray, its agents, representatives, or employees and you concerning any

transaction, account or the construction, performance or breach of this or any other agreement between us, whether entered into prior, on, or subsequent to the date hereof, shall be determined by arbitration to the full extent provided by law.

MONTANA FACIAL SURGERY PENSION AND PROFIT SHARING PLAN

18. Dr. Raymond Kaufman is the trustee of and a participant in the Montana Facial Surgery Pension and Profit Sharing Plan. The Plan opened an account with Piper Jaffray in 1988 with Dr. Kaufman signing a PAT account agreement. *Id.* at 78. The PAT agreement does not contain a requirement for pre-dispute arbitration. (See Exhibit D).

19. Dr. Kaufman never approached Piper in order to change the relationship between Piper and the Plan. *Id.* at 79.

20. Dr. Kaufman is an extremely busy physician who has little time to deal with his investment accounts. Mr. O'Neill was aware that Dr. Kaufman was exceedingly busy. Because of the demands on his time, Dr. Kaufman relied on O'Neill to explain what he needed to know about his investment accounts. *Id.* at 81.

21. O'Neill never explained anything to Dr. Kaufman regarding arbitration. *Id.* at 81.

22. The Montana Facial Surgery Pension and Profit Sharing Plan is an entirely separate and distinct entity from Dr. Kaufman individually. In addition to Dr. Kaufman, employees of the Facial Surgery clinic participated in the plan. Those employees withdrew from the plan before the events which give rise to this lawsuit.

Currently only Dr. Kaufman and his wife Janet Nothstine are participants in the plan. *Id.* at 82.

23. Whenever Dr. Kaufman was presented documents dealing with his own individual accounts he did not believe that those accounts had anything to do with the management of the Pension and Profit Plan. No one at Piper ever explained that by opening additional accounts that Dr. Kaufman could affect the rights of the Plan and its participants. *Id.*

24. All of the account documents that were presented to Dr. Kaufman were presented to him on a take-it-or-leave-it basis.

25. Dr. Kaufman signed a PAT Plus agreement for the Plan (Exhibit D) after he received it in the mail with a letter which stated that Piper was doing away with the type of account the Plan had. Further the letter explained that if the client did not sign the new account agreement that the Plan would be reassigned to a fee paying account format. The letter also recommends the PAT Plus account. (See Exhibit J to Piper's Brief in Support of its Motion to Compel Arbitration). Dr. Kaufman signed the agreement based upon Piper's recommendation to avoid being reassigned to a fee-paying account. *Id.* at 80. The PAT Plus account (Exhibit D) which Dr. Kaufman signed for the Plan also contains the language referred to in Finding number 16 above.

26. Dr. Kaufman never read the PAT Plus agreement but rather relied on Tom O'Neill to explain to him anything he needed to know about the agreement. *Id.* at 87.

27. O'Neill did not testify to refute the testimony of Ms. Nothstine or Dr. Kaufman yet he had the ability and opportunity to do so.

Findings Concerning Contract of Adhesion

28. The contracts at issue in the instant case are standardized form contracts, prepared by Piper Jaffray.

29. Piper Jaffray, because they controlled the Plaintiff's access to the securities market, had superior bargaining power in the transactions at issue herein relative to the Plaintiffs who were unsophisticated investors.

30. The provisions of these form contracts, and in particular the arbitration provisions, are drafted in accordance with industry practice and standards to conform to rules promulgated by the self-regulating organizations (SROs) that govern the entire securities industry. See Tr. Perino, 9/3/03, at 44, ll. 13-19.

31. These contracts and the arbitration provisions they contain are, on their face, contracts of adhesion, in that the form language provides no "opt-out" provision with regard to the arbitration clause, or any other contract provisions. Tr. Corbett, 8/12/03, at 60-61. The customer is provided no opportunity on the face of the document to select or consent to certain provisions, and not to others. A signature on the document purports to bind the consumer investors to all of the contract terms.

32. Piper did not call any employee from the Butte office to testify that they implemented or were even aware of the alleged "opt out" policy. O'Neill did not testify in this regard. English did not testify in this regard. The only witness who testified about the procedures in the Butte office was Jerry Campbell who was called by the Plaintiffs. Campbell testified that he was unaware of the alleged policy and that based upon his training and experience with Piper, the account documents were to be presented to investors on a take-it-or-leave-it basis. Given that Piper, O'Neill and English all had the ability to testify and

establish that the "opt out" policy was a part of the Butte operation and failed to do so and given the testimony of Jerry Campbell the court finds that there was no "opt out" policy in effect in the Butte office and that the account documents were presented to Butte investors (like the Plaintiff) on a take-it-or-leave-it basis.

33. These account forms, prepared by Piper Jaffray, were presented to the Plaintiffs on a "take it or leave it" basis, in accordance with the manner in which brokers are trained by Piper Jaffray to present these forms to their clients and prospective clients. *See* Tr. Campbell, 9/3/03, pg. 11

34. Moreover, the new PAT Plus forms presented to many of the plaintiffs for their signatures in 1993 were enclosed with a cover letter, advising that if the customers did not accept the terms of the new account forms, they would be transferred to a fee-paying account. Tr. Harmsen, 9/3/03, pgs. 213-215. Thus, not only were the contracts presented on a "take it or leave it" basis, but additionally, on a "take it or pay a fee" basis.

35. The letter, while purporting to advise customers of the essential new account terms, failed to inform the Butte branch customers that the new PAT Plus forms contained a pre-dispute arbitration clause, which for many customers, would be included within their account agreements for the first time. *Id.*

36. Plaintiffs herein had no bargaining power or meaningful opportunity to negotiate the terms of their contracts, including the arbitration provision.

37. Piper Jaffray's alleged "opt out" policy relating to the arbitration clause alone, but no other provisions in the form contracts, does not provide investors with a meaningful choice in opting out of the arbitration provision.

38. According to this alleged policy, branch managers are given discretion to permit a customer, at the customer's request, to cross out the arbitration clause in the account agreement forms. TR. Harmsen, pg. 172, hearing exhibit 4.

39. Piper does not apprise potential investors of the existence of the alleged "opt out" policy. Piper's investment executives who open new accounts in accordance with Piper Jaffray's policies, procedures and training do not inform or apprise their customers either of the existence of the arbitration clause, or of the alleged "opt out" policy. Tr. Harmsen, 9/3/03, 216, ll. 15-25. See also Tr. Campbell, 9/3/03, 11, ll. 17-25, and 12, ll. 1-7.

40. To be able to take advantage of this alleged "opt out" option, the Plaintiffs in this litigation would have had to have initiated the discussion with O'Neill, and questioned whether it would be possible to cross out the arbitration provision. Even then, the determination of whether this would be permissible would be made by the Branch Manager.

41. The alleged "opt out" policy was not known to the Butte branch office, from which the Plaintiffs' account originated. The Branch Manager (Bob English) and Mr. Campbell both had never heard of such a policy, and the so-called "policy" itself is centrally maintained in Minneapolis, and not distributed to the branches. Tr. Harmsen, 175-77. Tr. Campbell at pg. 8-12 and pg. 20. Tr. English (in Emett/Merritt hearing 8/8/2003 at pgs. 91-98).

42. It would have been impossible for the Butte office to have implemented the supposed opt-out policy with regard to the Plaintiffs in this litigation without having any knowledge of its existence, particularly in light of the fact that the option lies completely within

the discretion of the Butte branch managers, but the Butte branch manager had no knowledge whatsoever that he had such discretion.

43. Plaintiffs did not have reasonable notice of their supposed opportunity to negotiate or reject the arbitration clause. The contracts, on their face, provide no indication that the arbitration provision is optional, and can be crossed out. Piper Jaffray did not inform Plaintiffs that the arbitration provision was negotiable.

44. The Plaintiff [sic] in the instant litigation had no actual, meaningful or reasonable choice to negotiate or exercise any discretion with regard to the arbitration provision contained in the standardized Piper Jaffray form contracts.

45. Investors such as Plaintiffs face the possibility of being excluded from the securities market unless they accept Piper Jaffray's contract with such an agreement to arbitrate.

Findings Concerning Unconscionability

46. It is undisputed that under NASD and NYSE rules one of the three arbitrators must be affiliated with the securities industry. There is no requirement that an arbitrator must be affiliated with the industry in which the small investor, or "one time player," is employed. The securities industry will always have one third of the panel represented by it. There is clearly a disparity of representation which is inherently suspect. The securities industry itself has recognized that this disproportionate representation creates an appearance of pro-industry bias.

47. Repeat players are favored in securities arbitrations as opposed to workers or consumers who are unlikely

to be involved in arbitration more than one time. According to Professor William Corbett of the University of Montana Law School, who is a very experienced labor arbitrator in the Pacific Northwest, whose testimony the Court finds credible, empirical studies conducted by legal commentators have concluded that arbitrators tend to favor repeat players.

48. Filing fees for securities arbitration under NASD rules are substantial and far greater than the filing fees imposed in the Montana district courts. It is undisputed that the filing fees for such claims are in the range of $1,400 and $1,500, for a filing fee and a hearing deposit. This conclusion was not disputed by Piper's retained expert, Michael Perino. Fees at the rate of $450 per day for each additional day of a hearing would be charged.

49. Securities arbitration under the required NASD or NYSE rules impose significant arbitrator fees which make small claims prohibitive and discriminate against investors of modest means. In addition to the formal filing fees, an investor located in Montana would be required to either seek a waiver of the requirement that the arbitration be held in a state which has a NASD District Offices [sic], and then pay the lodging and travel expenses of the arbitrators who are required to travel from their states of residence to Montana, or pay the expenses of Montana witnesses who would be required to travel outside of Montana to testify.

50. Additionally, arbitrator fees are $400 per session day, plus $75 additional for the chairperson of the three-member panel, or $1,275 per day. Thus, if a case were to last five days, arbitrator fees alone would amount to $6,375, not to mention travel and related lodging expenses. In contrast, in the Montana district courts,

no litigant is required to pay for the daily fees or expenses of either judges or juries.

51. The NASD and NYSE rules require private arbitration proceedings, which result in summary decisions which provide no basis or opportunity for an explanation of the findings of the arbitrators, or the applicable law upon which the decision is based. These rules specifically preclude written decisions explaining their findings of fact and conclusions of law. Professor Corbett concluded that the failure to provide a written, explanatory decision is not only intentional, but touted as an "advantage" of arbitration because the decision makers are not "burdened" with the obligation to explain their decisions. There are no recognized public law reporting publications of securities decisions. This "penchant for secrecy" is an accepted feature of securities arbitration, and therefore frustrates a litigant's effort to seek a vacatur of the award in the courts, and may conceal an intentional disregard of the law. Additionally, as Professor Corbett points out, the failure to explain decision making may obscure biased or erroneous decision making. Securities arbitration proceedings thus become shrouded in secrecy because they are conducted in private forums which excludes public decision making. As a result, wrongdoing or other oppressive conduct by the securities industry or its members precludes any meaningful expose of such conduct and activities.

52. Securities arbitration is expressly designed to excuse arbitrators from being bound by the facts or law. It is expressly designed to preclude arbitrators from disclosing to the parties written reasons which would explain the basis of their decision. The pre-dispute arbitration provision at issue in this ease recites that –

> The arbitrators' award is not required to include factual findings or legal reasoning and any

> party's right of appeal to seek modification of rulings is strictly limited.

53. Many legal commentators have rightfully criticized the securities industry for insisting that its arbitration processes be expressly designed to preclude explanatory decisions which can serve as the basis of judicial review.

54. The pre-dispute arbitration provision, which is the subject of the motion to compel, severely limits the opportunity of claimants to discover facts necessary to prove a claim such as a company's business practices. This fact is stated clearly in Piper's own arbitration provision, to wit:

> Pre-arbitration discovery is generally more limited than and different from court proceedings.

Additionally securities industry arbitration rules discourage discovery except to a very limited extent. Depositions are "strongly discouraged", and limited to "exceptional circumstances". There has also been criticism of the limited role of discovery in arbitration cases, because securities firms can effectively "stonewall" discovery requests and delay production of information until the time of the hearing.

55. Because of the limited role of discovery in securities arbitration, the ability of a litigant to discovery matters not specifically related to the investor's account is severely compromised, making it difficult, if not impossible, to establish a company's business practice. In the instant case, allegations of improper business practices are central to Plaintiffs' tort claims and other claims surrounding the manner in which the Defendant Piper Jaffray and O'Neill conducted their business and the manner in which Piper supervised and encouraged O'Neill to maintain business practices previously determined to be improper. See Plaintiff's Complaint.

CONCLUSIONS OF LAW

PIPER'S BURDEN OF PROOF

1. The procedure for analyzing a Motion to Compel Arbitration is set forth in §27-5-115 MCA which provides in relevant part:

> **Proceedings to compel or stay arbitration.** (1) On the application of a party showing an agreement described in 27-5-114 and the opposing party's refusal to arbitrate, the district court shall order the parties to proceed with arbitration; but if the opposing party denies the existence of the agreement to arbitrate, the court shall proceed summarily to the determination of that issue raised and shall order arbitration if it finds for the applying party or deny the application if it finds for the opposing party.
>
> (2) On application, the district court may stay an arbitration proceeding commenced or threatened on a showing that there is no agreement to arbitrate. Such an issue, when in substantial and bona fide dispute, shall be immediately and summarily tried and file stay ordered if the court finds for the applying party. If the court finds for the opposing party, it shall order the parties to proceed to arbitration.

In this case, there exists a substantial and bona fide dispute concerning the enforceability of the alleged arbitration provisions. Pursuant to *Kingston v. Ameritrade, Inc.*, 2000 MT 269, 302 Mont. 90, 12 P.3d 929 this Court must therefore, conduct a hearing to obtain evidence to resolve the dispute. Such hearings have been held. Piper has the initial burden of establishing a valid agreement to arbitrate.

Fiduciary Duty Created by Piper's PAT Plus Agreement

2. In *Kloss v. Edward D. Jones* the Montana Supreme Court held that a fiduciary relationship is created whenever a broker has discretion to buy and sell securities in a client's account. The discretion to buy and sell can arise from the language in the account agreement. In *Kloss* the court found that the following language created a fiduciary duty on behalf of the broker and brokerage house:

> You may sell any and all property held in any of my accounts and cancel any open orders for the purchase or sale of any property without notice, in the event of my death or whenever in your discretion you consider it necessary for your protection.

Id. at paragraph 36.

3. The *Kloss* court also held that if a pre-dispute arbitration provision is contained in an agreement that creates a fiduciary relationship then the broker and brokerage house has a duty to explain the consequences of the pre-dispute arbitration provision they seek to enforce. *Id.* at paragraph 38.

4. The language contained in Piper's PAT Plus Agreement set forth in Finding of Fact number 16 creates a fiduciary duty on behalf of Piper and O'Neill to explain the consequences of the arbitration provision Piper seeks to enforce.

5. Because neither Piper nor O'Neill explained the consequences of the arbitration provision in the PAT Plus Agreements, those arbitration provisions are unenforceable.

Piper's Account Agreements are Contracts of Adhesion

6. A contract of adhesion is a contract whose terms are dictated by one contracting party to another who has no voice in its formation. *Kloss* at paragraph 24, citing Corbin on Contracts, section 1.4 at 13 (1993).

7. "Contracts of adhesion arise when a standardized form of agreement, usually drafted by the party having superior bargaining power, is presented to a party, whose choice is either to accept or reject the contract without the opportunity to negotiate its terms." *Kloss*, 2002 MT 129 ¶24 (quoting *Passage v. Prudential-Bache Securities, Inc.* (1986), 223 Mont. 60, 66, 727 P.2d 1298, 1301-02 (citations omitted)).

8. In *Passage v. Prudential-Bache Securities, Inc.* (1986), 223 Mont. 60, 727 P.2d 1298, the Montana Supreme Court described contracts of adhesion in the Securities context and the circumstances under which they are unenforceable as follows:

> . . . [T]he investor is faced with an industry wide practice of including Arbitration Clauses in standardized brokerage contracts. As the investor faces the possibility of being excluded from the securities market unless he accepts a contract with such an agreement to arbitrate, such clauses come within the adhesion doctrine. However, mere inequality in bargaining power does not render a contract unenforceable, nor are all standardized contracts unenforceable. As a consequence of current commercial realities, form forum clauses will control, absent a strong showing it should be set aside. For such a contract or clause to be void, it must fall within judicially imposed limits of enforcement. It will not be enforced against the weaker party when it is:

> (1) not within the reasonable expectations of said party or (2) within the reasonable expectations of the party, but, when considered in its context, is unduly oppressive, unconscionable, or against public policy. [Citations omitted.]

9. In contracts of adhesion, the contract terms are "dictated by one party to another who has no bargaining power and no realistic options." *Kloss*, 2002 MT 129 ¶24. If the party in the lesser bargaining position has no meaningful opportunity to negotiate or reject the terms of a contract, the contract is one of adhesion. *See Circuit City v. Mantor,* 335 F.3d 1101 (9th Cir. 2003) (applying California law).

10. "A meaningful opportunity to negotiate or reject the terms of a contract must mean something more than an empty choice. *At a minimum, a party must have reasonable notice of his opportunity to negotiate or reject the terms of a contract, and* he must have an actual, meaningful, and reasonable choice to exercise that discretion." *Circuit City v. Mantor,* 335 F.3d 1101, 1106 (9th Cir. 2003) (applying California law). (emphasis added).

11. Based upon the above Findings of Fact, the Court finds that Piper's account agreements are contracts of adhesion.

Piper's Pre-Dispute Arbitration Provision is Unconscionable

12. In *Kloss* the Court set forth the following 8 factors which this Court must examine in determining the issue of the conscionability of Piper's pre-dispute arbitration provision:

1. Are potential arbitrators disproportionately employed in one or the other party's field of business?

2. Do arbitrators tend to favor "repeat players" as opposed to workers or are unlikely to be involved in arbitration again? In other words, is there a tendency by arbitrators to avoid decisions which will result in the loss of future contracts for their services?

3. What are the filing fees for arbitration compared to the filing fees in Montana's district courts?

4. What are arbitrators' fees? Do they make small claims prohibitive? Do they discriminate against consumers or workers of modest means?

5. Are arbitration proceedings shrouded in secrecy so as to conceal illegal, oppressive or wrongful business practices?

6. To what extent are arbitrators bound by the law?

7. To what extent are arbitrators bound by the facts?

8. What opportunity do claimants have to discover the facts necessary to prove a claim such as a company's business practices?

13. Based upon the above Findings of Fact, the Court finds that Piper's pre-dispute arbitration provision is unconscionable and therefore unenforceable.

Piper's Pre-Dispute Arbitration Provision Was Not Within The Plaintiffs' Reasonable Expectations

14. Based upon Findings of Fact number 1 through 17, this Court finds that pre-dispute arbitration was not within the reasonable expectation of Janet Nothstine

as it relates to her regular IRA account and therefore Piper cannot enforce its alleged pre-dispute arbitration provisions contained in other account agreements.

15. Based upon Findings of Fact number [sic] 18 through 26 this Court finds that Raymond Kaufman did not reasonably expect that by signing account agreements in his own name that he was in any way affecting the rights of the Montana Facial Surgery Pension and Profit Sharing Plan. Therefore Piper cannot enforce the pre-dispute arbitration provisions contained in account documents not within the name of the Montana Facial Surgery Pension and Profit Sharing Plan.

Piper Has Failed to Demonstrate that the Plaintiffs Voluntarily, Knowingly, and Intelligently, Waived Their Constitutional Rights to a Jury Trial and Access the Courts

16. The right of trial by jury is secured, to all and shall remain inviolate. Article II, Section 26, Montana Constitution. This constitutionally guaranteed right is fundamental and deserving of the highest level of court scrutiny and protection. *State v. LaMere,* 2000 MT 45, 298 Mont. 358, 2 P.3d 204.

17. Courts of justice shall be open to every person and speedy remedy afforded for every injury to person, property, or character. Article II, Section 16 Montana Constitution. This right is as fundamental as any other Article II right because the right of access to the courts is included within the Constitution's Declaration of Right and without the right to access the courts other Article II rights would have little protection from infringement, and, thus, little meaning. *Kloss*, supra (Nelson, J. concurring) at ¶57.

18. Constitutional rights that cannot be enforced are illusory. *Id.* at ¶58.

19. A waiver of a fundamental right must be proven to have been made voluntarily, knowingly and intelligently – typically by the party seeking the waiver. *Id.* at ¶64.

20. Based upon Finding of Fact numbers 1 through 17 this Court finds that Piper has failed to demonstrate a voluntary, knowing and intelligent waiver by the Plaintiff Janet Nothstine of her constitutional right to access the courts and to a jury trial.

21. Based upon Finding of Fact number [sic] 18 through 26 this Court finds that Piper has failed to demonstrate a voluntary, knowing and intelligent waiver by the Plaintiff Raymond Kaufman as trustee of the Montana Facial Surgery Pension and Profit Sharing plan of his constitutional right to access the courts and to a jury trial.

CONCLUSION AND ORDER

The Defendant's Motion to Compel Arbitration and Stay Proceeding is denied.

DATED this 22nd day of April, 2004.

/s/ Thomas M. McKittrick
Thomas M. McKittrick
DISTRICT COURT JUDGE

Cc: William P. Joyce
Stanley T. Kaleczyc
John S. Lutz

MONTANA SECOND JUDICIAL DISTRICT COURT,
SILVER BOW COUNTY

RAYMOND KAUFMAN,
Individually and as Trustee of the
MONTANA FACIAL SURGERY
PENSION AND PROFIT PLAN
and JANET NOTHSTINE,

Plaintiffs,

vs. CAUSE NO. DV-02-16

U.S. BANCORP PIPER
JAFFRAY, INC., and
THOMAS J. O'NEILL
and JOHN DOES I AND X,

Defendants.

TRANSCRIPT OF THE PROCEEDINGS

Heard before the Honorable Thomas J. McKittrick

Silver Bow County Courthouse
Butte, Montana

July 24, 2003

* * *

[44] REDIRECT EXAMINATION

BY MR. BOYAR:

Q. Ms. Nothstine, I just have a couple questions for you.

In response to Mr. Joyce's questions, you stated that you believe the contracts that you signed were offered to you on a take-it-or-leave-it basis; is that right?

A. I didn't really think I had any way to refute anything, and I wouldn't have refuted anything, because I felt like he was working for my best interests.

Q. And you stated you felt like you didn't have any input into the contracts either; is that right?

A. Right.

Q. You never actually tried to negotiate any of the terms, did you?

A. Right.

Q. You never actually tried to negotiate any of the terms, did you?

A. No. I didn't try to negotiate anything.

Q. And I believe you also stated that you relied upon Tom O'Neill to explain things in the accounts; is that right?

A. Yes.

Q. But in all the accounts that you signed, he never explained anything about the accounts; is that true?

A. He never explained anything?

Q. He never went through the accounts and explained the account agreements to you; is that right?

[45] A. I don't remember anything about the account agreements, no. I remember my statements, when I asked questions about those.

Q. So you didn't expect him to review the items that were in the contracts he gave you.

A. No. If it was required to open the account, no, I didn't expect him to.

MR. BOYAR: I have no further questions, Your Honor.

MR. JOYCE: Your Honor, if I could have just one brief follow-up.

RECROSS-EXAMINATION

BY MR. JOYCE:

Q. Did you expect that Mr. O'Neill would explain what his role was as a broker to you, and did he?

A. His role as a broker?

Q. Yeah. You came to him, he was going to provide services; is that right?

A. Yes. And I figured he was legitimate, and I wouldn't have asked him to explain his role as a broker either.

Q. But I mean, in terms of what he could do for you, he did talk to you about those things from time to time, right? "We're going to invest in this, we're not going to invest in that," those sorts of things?

[46] A. Right.

Q. And there were times when he would present documents to you; is that right?

A. When I opened the accounts I can't remember other times.

Q. And during those times, did you expect that if there was something very important in it, that he'd point it out to you?

A. Yes.

MR. JOYCE: That's all I have.

FURTHER REDIRECT EXAMINATION

BY MR. BOYAR:

Q. Ms. Nothstine, I was just up here, and I thought you told me that you didn't expect Mr. O'Neill to explain items in the contracts that he gave you. Is that right?

A. I felt like, when I opened the account, if I wanted to open an account, I had to comply. Just like when you buy a house, they hand you 50 papers to sign. If you want to buy the house, or if you want to access a way to save money with a firm like Piper Jaffray, that you sign the papers to do that. And that's what I did.

Q. You mentioned buying a house. Even though some of those agreements might be form agreements with regard to a loan, you're aware you can ask them to give you a better interest rate, or something like that, correct?

[47] A. When we went to buy our house, they must have given us 70 papers, and they were all papers they wanted me to sign, and I signed them.

MR. JOYCE: Your Honor, I think we're getting a little far afield.

THE COURT: Sustained.

MR. JOYCE: Your Honor, I think wer're getting a little far afield.

MR. BOYER: I have no further questions.

THE COURT: You may step down.

Call your next witness.

MR. BOYER: Your Honor, I call to the stand Dr. Raymond Kaufman.

RAYMOND KAUFMAN, M.D.,

a plaintiff, having been first duly sworn,
testified upon his oath as follow:

DIRECT EXAMINATION

BY. MR. BOYER:

Q. Good afternoon, Dr. Kaufman. Could you please state your name for the record.

A. Raymond Kaufman.

Q. Your current address, please.

A. 3464 Burlington Street, Butte, Montana.

Q. And can you give me, briefly, your educational background.

A. I'm a physician.

Q. Which entailed medical school?

[48] A. Medical school, residency, fellowship.

Q. And how are you currently employed?

A. By Montana Facial Surgery.

Q. Could you trace your employment history for us briefly.

A. From what point?

Q. Just prior to – prior to entering college.

A. Prior to entering college?

Q. Yes.

A. That's when I did most of my work, so could you give me an idea of when?

Q. How about once you started working, then? Well, let me ask you this: You had some experience working on Wall Street; is that correct?

A. Yes.

Q. Can you explain what you did on Wall Street.

A. I was a clerk.

Q. And where were you a clerk?

A. Pickard & Company.

Q. Did you work anywhere else on Wall Street?

A. Smith, Jackson & Company.

Q. Anywhere else?

A. I did some part-time work for another firm. I don't remember the name.

Q. Approximately how long did you work on [49] Wall Street?

A. '67 to about '73.

Q. Dr. Kaufman, do you know Tom O'Neill?

A. Yes.

Q. How did you first meet Tom?

A. I'm not sure, but I think I was recommended to see him by my accountant.

Q. And do you know how many accounts that you had opened with Tom O'Neill?

A. One initially.

Q. I'm talking about – How many accounts in total did you open with Tom O'Neill?

A. IRA, Roth IRA, personal, joint, and pension and profit sharing plan.

Q. I just want to run through those with you. If you could refer to what's been previously marked as Defendant's Exhibit A.

(A brief discussion was held off the record.)

Q. Dr. Kaufman, if you could turn to the page that's marked PJ 13729.

THE COURT: This is exhibit –

MR. BOYER: This is Defendant's Exhibit A.

Q. Your signature is on this document?

A. Yes.

Q. And this is dated July 15th of '91; is that [50] right?

A. Yes.

Q. And this refers to a joint account that you and your wife had; is that correct?

A. I guess so.

Q. Do you recall opening up this account?

A. Yes.

Q. And what do you recall about it?

A. Opening the account.

Q. Do you recall any discussions with Tom O'Neill about the account agreement itself?

A. No.

Q. So do you recall reading the account agreement before signing?

A. No.

Q Do you know if you had the opportunity to read it?

A. I don't know if I had the opportunity read it.

Q. Do you have any reason to believe you weren't given an opportunity to read it.

A. Yes. I'm in terrible time constraints almost always, and these are usually done between something else, and I run in and run out.

Q. Now, when you say that, there's nothing that Tom O'Neill did or Piper did to deny you an opportunity to [51] read this, it would have been your own schedule; is that correct?

A. If I would have read it, I would have had to take it with me and come back some other time.

Q. So it was your own schedule, then?

A. Yes.

Q. So you don't recall Tom O'Neill discussing arbitration with regard to this account?

A. He did not.

Q. I'm sorry?

A. He did not.

Q. He did not, okay.

If you could flip to the page behind the ones we were just discussing, which is no PJ 13682. Again, at the bottom, your signature is on this page, correct?

A. Yes.

Q. And the date to the right of yours is February 2nd, '95; is that right?

A. Yes.

Q. This is an update, then, of the prior joint account; is that right?

A. I guess so.

Q. Do you recall how you came to open up this update?

A. This was sent to my home.

No. 04-454

IN THE SUPREME COURT OF THE STATE OF MONTANA

2005 MT 37

HARRY WILLEMS,

Plaintiff and Respondent,

v.

U.S. BANCORP PIPER JAFFRAY, INC., THOMAS J. O'NEILL, ROBERT ENGLISH, and JOHN DOES I through X

(Filed Feb. 22, 2005)

Defendants and Appellants.

APPEAL FROM:
District Court of the Second Judicial District,
In and For the County of Cause No. DV 2003-25
Honorable Kurt Krueger, Presiding Judge.

COUNSEL OF RECORD:

For Appellants:

Stanley T. Kaleczyc and Brand G. Boyar, Browning, Kaleczyc, Berry & Hoven, P.C., Helena, Montana

John S. Lutz, Fairfield and Woods, P.C., Denver, Colorado

Robert J. Phillips, Phillips & Bohyer, P.C., Missoula, Montana (O'Neill)

For Respondent:

William P. Joyce, Joyce & Johnston, PLLP, Butte, Montana

Submitted on Briefs: November 30, 2004
Decided: February 22, 2005

Filed:

Ed Smith
Clerk

Justice Jim Rice delivered the Opinion of the Court.

¶1 This case is one of 23 lawsuits filed by individual investors against U.S. Bancorp Piper Jaffray, Inc. (Piper), Robert English (English), and Tom O'Neill (O'Neill). The plaintiff investors made various common law tort claims arising from the alleged mismanagement of their accounts created and maintained by Piper's branch office in Butte, Montana. O'Neill, who was a securities broker in Piper's Butte office,[1] allegedly took the actions that gave rise to the lawsuits, and English was O'Neill's direct supervisor throughout this time. In response to the lawsuits, Piper filed motions to compel arbitration in each case, seeking to enforce "pre-dispute" arbitration clauses – that is, clauses in the account agreements which required any dispute be resolved by arbitration. Piper's motions to compel arbitration led to a series of hearings by a panel of three district court judges, who were sitting individually on the cases, but who sat *en banc* to hear evidence common to all 23 cases. In addition, individual hearings were held with respect to several of the individual plaintiffs. While Piper called common witnesses to testify, O'Neill, in a prior discovery deposition, invoked his Fifth Amendment right against self-incrimination and did not offer testimony regarding the accounts at issue.

[1] At the time the lawsuits were filed, O'Neill was no longer employed at Piper.

¶2 Harry Willems (Willems) is the plaintiff in this matter. On April 7, 2004, the Second Judicial District Court, Silver Bow County, denied Piper's motion to compel arbitration of Willems's claims, and Piper appeals therefrom. We affirm.

¶3 The following issues are raised on appeal in regard to the District Court's denial of Piper's motion to compel:

¶4 Did the District Court err in holding that the PAT Plus Agreements created a fiduciary duty between Piper and Willems that was breached by Piper?

¶5 Did the District Court violate the Federal Arbitration Act and Montana law by holding the arbitration agreement to a different contractual standard when it concluded the PAT Plus Agreements were contracts of adhesion?

¶6 Did the District Court err in applying the *Kloss* factors?

¶7 Did the District Court err in holding that Willems failed to effectively waive his constitutional rights?

¶8 Is the securities arbitration process, held before a self-regulatory organization overseen by the United States Securities and Exchange Commission, fair and reasonable as a matter of law?

¶9 The District Court's order offered an extensive analysis of all issues raised by the parties. The District Court determined that the PAT Plus Agreements were contracts of adhesion; that Piper's pre-arbitration dispute provisions were unconscionable and not within plaintiffs' reasonable expectations; that Piper failed to demonstrate that plaintiffs voluntarily, knowingly, and intelligently waived their constitutional rights to a jury trial and access to the court;

Piper failed to demonstrate that plaintiffs received or reviewed the arbitration provision; and that a fiduciary duty was created by Piper's PAT Plus Agreements and breached by the defendants. We conclude that the issue pertaining to the fiduciary duty is determinative on appeal and therefore will not address the other issues, except as necessary to resolve the dispositive issue.

FACTUAL AND PROCEDURAL BACKGROUND

¶10 In 1986. Willems retained O'Neill as his broker and financial advisor to help him open a Self-Directed Individual Retirement Account (1986 IRA). Later that year, Willems opened a joint Piper Automatic Transfer Account with his wife Marie Willems, which he later upgraded to a Co-Owner Piper Automatic Transfer Plus Account in 1995. On November 9, 1993, Willems opened a Co-Owner Piper Automatic Transfer Plus Account with his mother Bernice Willems. The 1993 and 1995 Piper Automatic Transfer Plus Account agreements hereinafter shall be collectively referred to as the "PAT Plus Agreements."

¶11 Willems claims that O'Neill, supervised by English, engaged in unlawful, unreasonable, and unethical conduct relating to the 1986 IRA, which did not contain a predispute arbitration clause. Willems contests Piper's invocation of the PAT Plus Agreements' arbitration clauses because: (1) his claims are not based upon transactions in these accounts; and (2) Willems was informed that the PAT Plus Agreements were entirely separate and distinct from his 1986 IRA, and therefore had no affect on his 1986 IRA. Conversely, Piper explains that by signing the PAT Plus Agreements, Willems agreed to arbitrate disputes

relating to *any* account he held with Piper, and notes the following language found in both PAT Plus Agreements:

> You agree to arbitrate **any disputes** between Piper Jaffray and you. You specifically agree and recognize that **all controversies** which may arise between Piper Jaffray, its agents, representatives or employees and you concerning any transaction, account of the construction, performance or breach of this or **any other agreement between us, whether entered into prior, on, or subsequent to the date hereof** shall be determined by arbitration to the full extent provided by law. [Emphasis added.]

Thus, it is the arbitration provisions, set forth in the PAT Plus Agreements and incorporating Willems's 1986 IRA, which are at issue herein.

¶12 On January 24, 2003, Willems filed a complaint in the Second Judicial District Court against Piper, English, and O'Neill alleging mismanagement of his 1986 IRA. On March 24, 2003, Piper filed a motion to compel arbitration based upon the provisions of the PAT Plus Agreements requiring arbitration of disputes in any of Willems's accounts. On July 9, August 12, and September 3, 2003, a panel of three district court judges sat *en banc* to hear evidence common to all 23 cases arising from the alleged misconduct of Piper's broker, O'Neill. On April 7, 2004, the District Court denied Piper's motion to compel arbitration and stay proceedings. Piper appeals therefrom.

STANDARD OF REVIEW

¶13 We review whether a district court's conclusions of law are correct in determining whether or not an issue is

subject to arbitration under an existing agreement. *Iwen v. U.S. West Direct*, 1999 MT 63, ¶ 17, 293 Mont. 512, ¶ 17, 977 P.2d 989, ¶ 17. When a district court is asked to compel arbitration of a dispute, the threshold inquiry is whether the parties agreed to arbitrate. *Solle v. Western States Ins. Agency*, 2000 MT 96, ¶ 22, 299 Mont. 237, ¶ 22, 999 P.2d 328, ¶ 22. Because arbitration is a matter of contract, the rules of contract apply, and a party cannot be required to submit to arbitration any dispute that the party has not agreed to submit. *Solle*, ¶¶ 22-23.

¶14 A fiduciary relationship is created whenever a broker has discretion to buy, sell, or otherwise control a client's account. *Chor v. Piper, Jaffray & Hopwood, Inc.* (1993), 261 Mont. 143, 153, 862 P.2d 26, 32. In determining the scope or extent of the fiduciary obligation, our review becomes highly fact intensive. *Kloss v. Edward D. Jones & Co.*, 2002 MT 129, ¶ 35, 310 Mont. 123, ¶ 35, 54 P.3d 1, ¶ 35.

DISCUSSION

¶15 Did the District Court err in holding that the PAT Plus Agreements created a fiduciary duty between Piper and Willems that was breached by Piper?

¶16 In *Chor*, we held that § 30-10-301(1), MCA, creates an implied code of conduct for brokers, violations of which may constitute a breach of the duty that a broker owes to his customer. *Chor*, 261 Mont. at 152, 862 P.2d at 31-32. We further held that in the absence of discretionary authority by a broker to buy and sell in a customer's account, no fiduciary relationship is created between the broker and the customer. *Chor*, 261 Mont. at 153, 862 P.2d

at 32. In *Kloss*, we inversely restated that principle, holding that "a fiduciary relationship *is created* whenever a broker has discretion to buy and sell in the client's account." *Kloss*, ¶35. Thus, we begin our analysis by first determining whether the PAT Plus Agreements granted such discretion to Piper's brokers.

¶17 Piper argues that the PAT Plus Agreements did not grant it discretion to make trades on behalf of its clients and therefore did not create a fiduciary duty. Piper contends the District Court improperly interpreted the following underlined contract provisions:

> **Customer's Orders Binding Until Notice of Death**
>
> Upon your death or failure to comply with any part of this Agreement or *whenever Piper Jaffray deems it necessary for its protection, Piper Jaffray is authorized (but is not required) to:*
>
> – Cancel outstanding orders;
>
> – *Purchase, sell, assign, receive and deliver all or any part of the securities held or carried for you*; and
>
> – Close out short sales by purchase upon any exchange board or market or any public or private sale at Piper Jaffray's option.

(Underlining added.) In particular, Piper claims that the phrase, "whenever Piper Jaffray deems it necessary for its protection," concerns Piper's rights upon a client's death or when a client is otherwise incapacitated. Piper makes note that upon the death or incapacity of a client, it must have a limited discretion over the client's accounts in case the securities decline in value so that it may ensure it is in

compliance with certain federal requirements, but that this limited discretion is not sufficient to trigger discretion for purposes of creating a fiduciary duty. Thus, Piper urges this Court to not derive a "broad" or "unfettered" grant of discretion from the middle of a provision that merely concerns Piper's rights upon the death or incapacitation of a client.

¶18 Additionally, Piper notes that its Supervisory Procedures Manual provides that a client must execute additional documents if the client wishes to grant discretion to Piper. Piper claims that Willems did not execute the required documentation according to the procedures in the supervisory manual. Piper argues that the fact that Willems's claims include allegations that Piper made "unauthorized transactions" in his 1986 IRA, a nondiscretionary account, is additional evidence that Willems understood that Piper lacked discretion to independently authorize transactions.

¶19 Finally, Piper argues that *Kloss* does not control the outcome here for two reasons. First, Piper asserts that the brokerage account agreement in *Kloss* is distinguishable from the PAT Plus Agreements. Second, it argues that the *Kloss* holding that a broker has a fiduciary duty to disclose and explain the arbitration clause within the account agreement is "in contrast to most statements of law." Piper contends that if a broker had discretion in handling an account, the broker's duties would not extend beyond financial management. Furthermore, Piper claims that brokers should not have the duty to read and explain arbitration clauses to clients since clients come to brokers for financial advice, not legal advice, and the broker may be engaging in the unauthorized practice of law.

¶20 Piper's second *Kloss* argument is essentially an invitation to revisit and reverse our holding in *Kloss*. However, we see no error in the *Kloss* Court's analysis as to the fiduciary duty in this context, and therefore, we decline Piper's invitation to revisit that decision. We reject Piper's argument that such discretion does not create a fiduciary obligation to explain the arbitration provisions, or that such an obligation requires the broker to engage in the unauthorized practice of law. The obligation is one which accompanies the fiduciary relationship created when a broker accepts a customer's authorization to make transactions within the customer's account in the broker's own discretion.

¶21 Willems responds to Piper's first *Kloss* argument by arguing that the language highlighted in the PAT Plus Agreements is similar to the language in the *Kloss* agreement, which provided:

> You may sell any or all property held in any of my accounts and cancel any open orders for the purchase or sale of any property without notice, in the event of my death or whenever in your discretion you consider it necessary for your protection.

Kloss, ¶ 36. We determined that this language granted discretion to the broker to buy and sell securities on behalf of the broker's client. *Kloss*, ¶¶ 36-37. Thus, Willems asserts the District Court properly concluded that the similar language in the PAT Plus Agreements likewise granted such discretion, thereby creating a fiduciary duty on behalf of the broker to explain the consequences of arbitration to clients.

¶22 In spite of Piper's contention that it is required under federal law to have "limited discretion" to make transactions on behalf of its clients to ensure compliance with certain federal requirements, the PAT Plus Agreements contain no provisions or explanations as to this "limitation" or that the discretion granted in the agreement is effective only when securities decline in value. Moreover, the plain meaning of the following language – "upon your death **or** failure to comply with any part of this Agreement **or** whenever Piper Jaffray deems it necessary for its protection" – demonstrates that Piper retained broad authority to purchase, sell, assign, receive and deliver all or any part of the securities held by its clients. (Emphasis added.) Indeed, transactions could be made whenever Piper "deem[ed] it necessary" for its own best interest. Thus, the District Court did not err in concluding that the PAT Plus Agreements granted Piper's brokers discretion to buy and sell securities thereby creating a fiduciary duty.

¶23 Piper contends that the District Court erroneously concluded that a fiduciary duty existed before Willems signed the PAT Plus Agreements. Piper explains that written contracts are only effective at delivery, and therefore a fiduciary duty, triggering an obligation to explain the arbitration provision, could not exist before the PAT Plus Agreements were signed. Willems responds that Piper's argument is misplaced in view of our holding in *Kloss*. Willems argues that when a fiduciary duty is created, even if it is created the very moment *after* the agreement is signed, a broker has a duty to advise its customers – pursuant to its duty of the finest loyalty – as to the nature of arbitration, or if the client may "opt out" of arbitration by crossing out the provision.

¶24 In *Kloss*, an investor opened an account which contained a pre-dispute arbitration clause. We concluded that, because the brokerage firm had discretion to buy and sell securities in the investor's account, a fiduciary relationship was created and the broker had an obligation to explain the effect of an arbitration clause. *Kloss*, ¶ 37. Although we did not state that the obligation arose prior to the actual signing of the agreement, that was, by necessity, the effect of our holding. Entering an agreement which bestows discretion upon the broker requires that the customer be advised of the agreement's arbitration provision so that an informed decision to sign the agreement can be made.

¶25 It is undisputed that Piper did not advise Willems as to the nature of the arbitration clause or that he had the option of crossing out certain provisions. Further, the District Court found, and Piper does not challenge on appeal, that Willems did not understand that by signing the PAT Plus Agreements he was in any way affecting his 1986 IRA. Therefore, in accordance with our holding in *Kloss*, we conclude the District Court did not err in holding that the PAT Plus Agreements created a fiduciary duty between Piper and Willems and that Piper breached its fiduciary duty when it failed to explain the consequences of the arbitration provision prior to the formation of the contract.

¶26 Finally, Piper contends that, pursuant to the *Kloss* Court's determination that the analysis as to whether a fiduciary duty exists is "highly fact intensive," the facts here are distinguishable from those in *Kloss*. It notes that, in *Kloss*, the broker had a regular practice of explaining key contract terms to the customer, and that this led the Court to conclude that the broker had a fiduciary duty to

explain the arbitration provision to the customer. Piper thus reasons that the District Court improperly relied on *Kloss* to create a "special legal standard" regarding fiduciary duties applicable only to arbitration provisions and not to other contract provisions, in violation of the Federal Arbitration Act (FAA) and United States Supreme Court precedent.

¶27 We conclude that the District Court created no new special legal standards but instead properly applied Montana case law by relying on *Kloss*. "The FAA provides that an agreement to arbitrate is valid except where grounds exist at law or in equity to revoke the contract. . . . Montana law also requires the enforcement of predispute arbitration clauses 'except upon grounds that exist at law or in equity for the revocation of a contract.' *Kingston v. Ameritrade, Inc.*, 2000 MT 269, ¶ 13, 302 Mont. 90, ¶ 13, 12 P.3d 929, ¶ 13 (citing § 27-5-114(2), MCA). Though the brokerage firm in *Kloss* had a "regular practice of explaining key contract terms," the enforceability of an arbitration provision is not dependent upon such an office custom or practice. The determination of the existence of a duty here is dependent upon all of the facts, and particularly, the extent of authority or discretion granted by the customer within the agreement.

¶28 We affirm the District Court's conclusion that Piper owed a fiduciary duty to explain the arbitration provision to Willems which was breached, and further, that the predispute arbitration provisions in the PAT Plus Agreements are unenforceable.

/s/ Jim Rice
Justice

We Concur:

/s/ James C. Nelson

/s/ Patricia Cotter

/s/ John Warner

/s/ W. William Leaphart

Justices

KURT KRUEGER
DISTRICT COURT JUDGE, DEPT. I
SILVER BOW COUNTY COURTHOUSE
155 W. GRANITE ST.
BUTTE, MT 59701
406/497-6410

MONTANA SECOND JUDICIAL DISTRICT COURT,
SILVER BOW COUNTY

HARRY WILLEMS,	*	
Plaintiff,	*	
vs.	*	**CAUSE NO. DV-03-25**
U.S. BANCORP PIPER JAFFRAY, INC., THOMAS J. O'NEILL, ROBERT ENGLISH & JOHN DOES I through X,	*	**FINDINGS OF FACT, CONCLUSIONS OF LAW & ORDER**
	*	(Filed Apr. 7, 2004)
Defendants.	*	

INTRODUCTION

Almost two dozen individuals who were investors with Piper Jaffray (Piper) at its Branch Office in Butte, Montana, have filed suits in the above-referenced cases against Piper as a result of its business practices and those of its account executive, Tom O'Neill. The lawsuits involve the investors' individual investment accounts which were created and maintained at the Butte office. While, of course, the circumstances surrounding the opening and maintenance of these accounts vary somewhat among those Plaintiffs, there is a similar, if not identical, fact pattern with respect to the essential facts surrounding the actual creation and maintenance of those accounts. Plaintiffs allege a number of common law tort claims which

arise from a variety of illegal business practices, such as "churning," unauthorized trading, and inappropriate trading. Plaintiffs allege that Piper failed to properly supervise O'Neill, who was at the time of his misconduct was subject to a Consent Decree with the Montana State Auditor. The decree arose out of prior misconduct of O'Neill which had been uncovered following an administrative investigation in the early 1990s. Piper had a duty to supervise O'Neill to insure that his misconduct and unethical practices as a broker would not be repeated. Plaintiffs allege that Piper not only allowed, but encouraged, O'Neill to repeat the proscribed business practices which had given rise to the Consent Decree.

Defendants have filed Motions to Compel Arbitration in all of the above-referenced cases. The motions gave rise to a series of hearings by the three Montana District Court Judges to whom these Piper cases have been assigned, Hon. Kurt Krueger, Hon. John W. Whelan, and Hon. Thomas M. McKittrick. Individual hearings took place with respect to many of the Plaintiffs who have a pending claim against Piper. Additionally, the three judges, sitting in an *en banc* configuration, heard the testimony, and received evidence, from "common expert witnesses" and "common fact witnesses." Those "common witness" hearings took place on August 12, 2003, and September 3, 2003, at which Plaintiffs called Professor William Corbett as a common expert witness. Plaintiffs called Jerry Campbell, a former Piper account executive, as a common fact witness. Defendants called Michael Perino, of New York, and Wendy Harmsen, of Minneapolis, as common expert and fact witnesses, respectively.

In a prior discovery deposition, Defendant Tom O'Neill refused to respond to questioning regarding the opening

and formation of Plaintiffs' accounts, citing his Fifth Amendment right against self-incrimination. Thus, there was no testimony presented by Defendants to refute the testimony of any Plaintiff with regard to the opening and maintenance of the account documents which they had signed which contained the pre-dispute arbitration clauses which are the basis of Defendants' motion to compel arbitration.

Following the conclusion of these common hearings, the parties submitted their post-hearing briefs on October 10, 2003.

FINDINGS OF FACT

Findings of Fact Specific for this Plaintiff

1. The Plaintiff Harry Willems is an unsophisticated retired Anaconda Company employee with less than an eighth grade education. (TR, Willems, 7/9/03, pg. 21).

2. Because of his lack of sophistication and education, Mr. Willems was not capable of understanding the language used in Piper's account agreements including the language in the arbitration provision. *Id.*

3. Mr. Willems' dealings with O'Neill date back to the 1980's when O'Neill was with DA Davidson. O'Neill took the account from DA Davidson to Piper when he moved to Piper. *Id.* at 23.

4. Based upon Mr. Willems' testimony and demeanor in court it is apparent that Mr. Willems is a person of limited intelligence. This fact would have been apparent to O'Neill after his first meeting with Mr. Willems. O'Neill was aware that Mr. Willems was unsophisticated and had only an 8th grade education. *Id.* at 24.

5. Because of his lack of intelligence and extreme lack of sophistication, Mr. Willems relied on O'Neill to explain beforehand the purpose of the documents he asked Mr. Willems to sign and O'Neill did speak with Mr. Willems about the purpose of the documents he needed Mr. Willems to sign before Mr. Willems was asked to sign the documents. *Id.* at 32.

6. The current litigation involves mismanagement of Mr. Willems' IRA account. *Id.* at 27. Mr. Willems opened the IRA account in March of 1986. The account agreement concerning the IRA does not require that Mr. Willems submit to binding arbitration concerning his IRA. See Plaintiff's Exhibit 1.

7. Mr. Willems had two other accounts with Piper Jaffray. One, a joint PAT Plus account agreement with his mother Bernice Willems (Exhibit A) and another a joint PAT Plus account agreement with his wife Marie (Exhibit B).

8. Both of the PAT Plus account agreements begin with the following language:

> This agreement ("Agreement") sets forth the terms and conditions governing the Piper Jaffray PAT Plus Account ("PAT Plus Account") offered by Piper Jaffray Inc. ("Piper Jaffray"), for which you (all such signatories hereto, whether acting in their individual or representative capacities, are sometimes referred to as "you") are making application with Piper Jaffray.

This language is inconsistent with the following language in the Pre-dispute Arbitration provision which suggests that the account agreement applies to other accounts:

> You agree to arbitrate any disputes between Piper Jaffray and you. You specifically agree

> and recognize that all controversies which may arise between Piper Jaffray, its agents, representatives, or employees and you concerning any transaction, account or the construction, performance or breach of this or any other agreement between us, whether entered into prior, on, or subsequent to the date hereof, shall be determined by arbitration to the full extent provided by law.

9. The PAT Plus account agreements also contain the following language which confers discretion on Piper:

> b. "Upon your death or failure to comply with any part of this Agreement *or whenever Piper Jaffray deems it necessary for its protection, Piper Jaffray is authorized (but is not required) to:*
>
> - Cancel outstanding orders;
> - *Purchase, sell, assign, receive and deliver all or any part of the securities held or carried for you;* and
> - Close out short sales by purchase upon any exchange board or market or any public or private sale at Piper Jaffray's option. (Emphasis added) (See Exhibit A)

10. Neither O'Neill nor anyone else at Piper ever advised Mr. Willems about the consequences of the pre-dispute arbitration provisions. Mr. Willems did not understand that the arbitration provisions existed until he spoke with his lawyer during this litigation. *Id.* at 32.

11. When Mr. Willems signed the two PAT Plus agreements he did not know that these accounts contained arbitration. Further, Mr. Willems understood that the joint account with his mother and the joint account

with his wife were separate and distinct accounts and he did not believe that by signing documents relating to these two accounts that he was in any way affecting his IRA account. *Id.* at 28.

12. Mr. Willems signed the joint PAT Plus account with his mother Bernice (Exhibit A) at the urging of O'Neill who told Mr. Willems that this was necessary to look after Mr. Willems' mother. *Id* at 29. This was done because Mr. Willems' mother had become very sick and could not take care of her business anymore and O'Neill told Mr. Willems that he should put his name on the account to make sure that his mother's money could be looked after. *Id.* at 11. Mr. Willems was concerned that if his name was not put on the account that his mother would be conned out of her money. *Id.* at 28.

13. When Mr. Willems had his name placed on his mother's account he did not expect that this was in any way affecting his rights vis-a-vis his IRA in that he understood that those accounts were separate and distinct accounts. *Id.* at 29.

14. When counsel for Piper read portions of the arbitration provisions contained in the PAT Plus account agreements, it was apparent to the Court that Mr. Willems did not understand the language used and Mr. Willems clearly indicated that he did not understand the arbitration provision. In his words, it was all "Greek to me". *Id.* at 15.

15. O'Neill took steps to gain Mr. Willems' trust. He repeatedly advised Mr. Willems that he was looking after his accounts just like he looked after his dad's accounts. O'Neill even made reference to a small notebook on his desk which supposedly contained the names of O'Neill's dad and Mr. and Mrs. Willems. O'Neill would make reference to this notebook and

advised Mr. Willems that he checked the stocks of the peoples whose name were in the notebook everyday and that Mr. Willems did not need to worry. *Id.* at 23. O'Neill further told Mr. Willems that he would check his stock every day just like he checked the stocks of his dad. Based upon these representations Mr. Willems came to trust O'Neill. *Id.* at 24.

16. Mr. Willems and his wife Marie made it clear to O'Neill that they wanted the joint account invested conservatively in a money market account and not in the stock market. O'Neill assured Mr. Willems that the joint account with his wife would be kept entirely separate from his IRA. O'Neill never told Mr. Willems or his wife when they opened up the joint money market account that it would in any way effect his IRA. Mr. Willems understood that the money market account was completely separate from the IRA and this was the only reason Mr. Willems and his wife opened the joint PAT Plus account. *Id.* at 30.

17. Mr. Willems understood that the IRA account had specific rules that did not allow him to make withdrawals whenever he wanted. The joint account, in contrast, could be accessed by he and his wife at any time. These differences in rules regarding access to the accounts provide further support for Mr. Willems' reasonable belief that in signing the PAT Plus account agreement he was not affecting his rights vis-a-vis his IRA.

18. O'Neill did not testify at the hearing although he had the ability and opportunity to do so.

Findings Concerning Contract of Adhesion

19. The contracts at issue in the instant case are standardized form contracts, prepared by Piper Jaffray.

20. Piper Jaffray, because they controlled the Plaintiffs access to the securities market, had superior bargaining power in the transactions at issue herein relative to the Plaintiff who was an unsophisticated investor.

21. The provisions of these form contracts, and in particular the arbitration provisions, are drafted in accordance with industry practice and standards to conform to rules promulgated by the self-regulating organizations (SROs) that govern the entire securities industry. *See* Tr. Perino, 9/3/03, at pg. 44.

22. These contracts and the arbitration provisions they contain are, on their face, contracts of adhesion, in that the form language provides no "opt-out" provision with regard to the arbitration clause, or any other contract provisions. Tr. Corbett, 8/12/03, at pgs. 60-61. The customer is provided no opportunity on the face of the document to select or consent to certain provisions, and not to others. A signature on the document purports to bind the consumer investors to all of the contract terms.

23. Piper did not call any employee from the Butte office to testify that they implemented or were even aware of the alleged "opt out" policy. O'Neill did not testify in this regard. English did not testify in this regard. The only witness who testified about the procedures in the Butte office was Jerry Campbell who was called by the Plaintiffs. Campbell testified that he was unaware of the alleged policy and that based upon his training and experience with Piper, the account documents were to be presented to investors on a take-it-or-leave-it basis. Given that Piper, O'Neill and English all had the ability to testify and establish that the "opt out" policy was a part of the Butte operation and failed to do so and given the testimony of Jerry Campbell the court finds that there was no "opt out" policy in effect in the Butte office and that the account documents

were presented to Butte investors (like the Plaintiff) on a take-it-or-leave-it basis.

24. These account forms, prepared by Piper Jaffray, were presented to the Plaintiffs on a "take it or leave it" basis, in accordance with the manner in which brokers are trained by Piper Jaffray to present these forms to their clients and prospective clients. *See* Tr. Campbell, 9/3/03, pg. 11.

25. Moreover, the new PAT Plus forms presented to many of the plaintiffs for their signatures in 1993 were enclosed with a cover letter, advising that if the customers did not accept the terms of the new account forms, they would be transferred to a fee-paying account. Tr. Harmsen, 9/3/03, at pgs. 213-215. Thus, not only were the contracts presented on a "take it or leave it" basis, but additionally, on a "take it or pay a fee" basis.

26. The letter, while purporting to advise customers of the essential new account terms, failed to inform the Butte branch customers that the new PAT Plus forms contained a pre-dispute arbitration clause, which for many customers, would be included within their account agreements for the first time. *Id.*

27. Plaintiffs herein had no bargaining power or meaningful opportunity to negotiate the terms of their contracts, including the arbitration provision.

28. Piper Jaffray's alleged "opt out" policy relating to the arbitration clause alone, but no other provisions in the form contracts, does not provide investors with a meaningful choice in opting out of the arbitration provision.

29. According to this alleged policy, branch managers are given discretion to permit a customer, at the customer's request, to cross out the arbitration clause in

the account agreement forms. TR. Harmsen, 172, Hearing Exhibit 4.

30. Piper does not apprise potential investors of the existence of the alleged "opt out" policy. Piper's investment executives who open new accounts in accordance with Piper Jaffrays policies, procedures and training do not inform or apprise their customers either of the existence of the arbitration clause, or of the alleged "opt out" policy. Tr. Harmsen, 9/3/03, pg. 216. *See* also Tr. Campbell, 9/3/03, pgs. 11 and 12.

31. To be able to take advantage of this alleged "opt out" option, the Plaintiffs in this litigation would have had to have initiated the discussion with O'Neill, and questioned whether it would be possible to cross out the arbitration provision. Even then, the determination of whether this would be permissible would be made by the Branch Manager.

32. The alleged "opt out" policy was not known to the Butte branch office, from which the Plaintiffs' account originated. The Branch Manager (Bob English) and Mr. Campbell both had never heard of such a policy, and the so-called "policy" itself is centrally maintained in Minneapolis, and not distributed to the branches. Tr. Harmsen, pgs. 175-77. Tr. Campbell at pgs. 8-12 and pg. 20. Tr. English, (in Emett/Merrett hearing), 8/8/2003 pgs. 91-98.

33. It would have been impossible for the Butte office to have implemented the supposed opt-out policy with regard to the Plaintiffs in this litigation without having any knowledge of its existence, particularly in light of the fact that the option lies completely within the discretion of the Butte branch managers, but the Butte branch manager had no knowledge whatsoever that he had such discretion.

34. Plaintiffs did not have reasonable notice of their supposed opportunity to negotiate or reject the arbitration clause. The contracts, on their face, provide no indication that the arbitration provision is optional, and can be crossed out. Piper Jaffray did not inform Plaintiffs that the arbitration provision was negotiable.

35. The Plaintiff in the instant litigation had no actual, meaningful or reasonable choice to negotiate or exercise any discretion with regard to the arbitration provision contained in the standardized Piper Jaffray form contracts.

36. Investors such as Plaintiffs face the possibility of being excluded from the securities market unless they accept Piper Jaffray's contract with such an agreement to arbitrate.

Findings Concerning Unconscionability

37. It is undisputed that under NASD and NYSE rules one of the three arbitrators must be affiliated with the securities industry. There is no requirement that an arbitrator must be affiliated with the industry in which the small investor, or "one time player," is employed. The securities industry will always have one third of the panel represented by it. There is clearly a disparity of representation which is inherently suspect. The securities industry itself has recognized that this disproportionate representation creates an appearance of pro-industry bias.

38. Repeat players are favored in securities arbitrations as opposed to workers or consumers who are unlikely to be involved in arbitration more than one time. According to Professor William Corbett of the University of Montana Law School, who is a very experienced labor arbitrator in the Pacific Northwest, whose testimony

the Court finds credible, empirical studies conducted by legal commentators have concluded that arbitrators tend to favor repeat players.

39. Filing fees for securities arbitration under NASD rules are substantial and far greater than the filing fees imposed in the Montana district courts. It is undisputed that the filing fees for such claims are in the range of $1,400 and $1,500, for a filing fee and a hearing deposit. This conclusion was not disputed by Piper's retained expert, Michael Perino. Fees at the rate of $450 per day for each additional day of a hearing would be charged.

40. Securities arbitration under the required NASD or NYSE rules impose significant arbitrator fees which make small claims prohibitive and discriminate against investors of modest means. In addition to the formal filing fees, an investor located in Montana would be required to either seek a waiver of the requirement that the arbitration be held in a state which has a NASD District Offices, and then pay the lodging and travel expenses of the arbitrators who are required to travel from their states of residence to Montana, or pay the expenses of Montana witnesses who would be required to travel outside of Montana to testify.

41. Additionally, arbitrator fees are $400 per session day, plus $75 additional for the chair person of the three-member panel, or $1,275 per day. Thus, if a case were to last five days, arbitrator fees alone would amount to $6,375, not to mention travel and related lodging expenses. In contrast, in the Montana district courts, no litigant is required to pay for the daily fees or expenses of either judges or juries.

42. The NASD and NYSE rules require private arbitration proceedings, which result in summary decisions

which provide no basis or opportunity for an explanation of the findings of the arbitrators, or the applicable law upon which the decision is based. These rules specifically preclude written decisions explaining their findings of fact and conclusions of law. Professor Corbett concluded that the failure to provide a written. explanatory decision is not only intentional, but touted as an "advantage" of arbitration because the decision makers are not "burdened" with the obligation to explain their decisions. There are no recognized public law reporting publications of securities decisions. This "penchant for secrecy" is an accepted feature of securities arbitration, and therefore frustrates a litigant's effort to seek a vacatur of the award in the courts, and may conceal an intentional disregard of the law. Additionally, as Professor Corbett points out, the failure to explain decision making may obscure biased or erroneous decision making. Securities arbitration proceedings thus become shrouded in secrecy because they are conducted in private forums which excludes public decision making. As a result, wrongdoing or other oppressive conduct by the securities industry or its members precludes any meaningful expose of such conduct and activities.

43. Securities arbitration is expressly designed to excuse arbitrators from being bound by the facts or law. It is expressly designed to preclude arbitrators from disclosing to the parties written reasons which would explain the basis of their decision. The pre-dispute arbitration provision at issue in this case recites that:

> The arbitrators' award is not required to include factual findings or legal reasoning and any party's right of appeal to seek modification of rulings is strictly limited.

44. Many legal commentators have rightfully criticized the securities industry for insisting that its arbitration processes be expressly designed to preclude explanatory decisions which can serve as the basis of judicial review.

45. The pre-dispute arbitration provision, which is the subject of the motion to compel, severely limits the opportunity of claimants to discover facts necessary to prove a claim such as a company's business practices. This fact is stated clearly in Piper's own arbitration provision, to wit:

> Pre-arbitration discovery is generally more limited than and different from court proceedings.

Additionally, securities industry arbitration rules discourage discovery except to a very limited extent. Depositions are "strongly discouraged", and limited to "exceptional circumstances". There has also been criticism of the limited role of discovery in arbitration cases, because securities firms can effectively "stonewall" discovery requests and delay production of information until the time of the hearing.

46. Because of the limited role of discovery in securities arbitration, the ability of a litigant to discovery matters not specifically related to the investor's account is severely compromised, making it difficult, if not impossible, to establish a company's business practice. In the instant case, allegations of improper business practices are central to Plaintiffs' tort claims and other claims surrounding the manner in which the Defendant Piper Jaffray and O'Neill conducted their business and the manner in which Piper supervised and encouraged O'Neill to maintain business practices previously determined to be improper. See Plaintiff's Complaint.

CONCLUSIONS OF LAW

Piper's Burden of Proof

1. The procedure for analyzing a Motion to Compel Arbitration is set forth in §27-5-115 MCA which provides in relevant part:

> Proceedings to compel or stay arbitration. (1) On the application of a party showing an agreement described in 27-5-114 and the opposing party's refusal to arbitrate, the district court shall order the parties to proceed with arbitration; but if the opposing party denies the existence of the agreement to arbitrate, the court shall proceed summarily to the determination of that issue raised and shall order arbitration if it finds for the applying party or deny the application if it finds for the opposing party; (2) On application, the district court may stay an arbitration proceeding commenced or threatened on a showing that there is no agreement to arbitrate. Such an issue, when in substantial and bona fide dispute, shall be immediately and summarily tried and the stay ordered if the court finds for the applying party. If the court finds for the opposing party, it shall order the parties to proceed to arbitration.

In this case, there exists a substantial and bona fide dispute concerning the enforceability of the alleged arbitration provisions. Pursuant to *Kingston v. Ameritrade, Inc.,* 2000 MT 269, 302 Mont. 90, 12 P.3d 929 this Court must therefore, conduct a hearing to obtain evidence to resolve the dispute. Such hearings have been held. Piper has the initial burden of establishing a valid agreement to arbitrate.

Fiduciary Duty Created by Piper's PAT Plus Agreement and O'Neill's Representations

2. In *Kloss v. Edward D. Jones* the Montana Supreme Court held that a fiduciary relationship is created whenever a broker has discretion to buy and sell securities in a client's account. The discretion to buy and sell can arise from the language in the account agreement. In *Kloss* the court found that the following language created a fiduciary duty on behalf of the broker and brokerage house:

> You may sell any and all property held in any of my accounts and cancel any open orders for the purchase or sale of any property without notice, in the event of my death or whenever in your discretion you consider it necessary for your protection. *Id.* at paragraph 36.

3. The *Kloss* court also held that if a pre-dispute arbitration provision is contained in an agreement that creates a fiduciary relationship then the broker and brokerage house has a duty to explain the consequences of the pre-dispute arbitration provision they seek to enforce. *Id.* at paragraph 38.

4. The language contained in Piper's PAT Plus Agreements set forth in Finding of Fact number 9 creates a fiduciary duty on behalf of Piper and O'Neill to explain the consequences of the arbitration provisions Piper seeks to enforce.

5. The scope of or extent of a fiduciary obligation depends on the facts of the case. *Kloss,* supra at ¶ 31, In *Deist v. Wacholz,* 208 Mont. 207, 678 P.2d 188 (1984) the Montana Supreme Court found that a fiduciary duty arose when a bank officer undertook to provide financial advise [sic] to an elderly customer concerning the sale of her ranch. Because of Mr. Willems extreme unsophistication and lack of education which

O'Neill was aware of and because of the representation that O'Neill made about looking after his accounts like he did his father's account, O'Neill established a fiduciary relationship with Mr. Willems which also gives rise to the duty to explain arbitration.

6. Because neither Piper nor O'Neill explained the consequences of the arbitration provision in the PAT Plus Agreements and because of the existence of the fiduciary duty, Piper cannot now enforce those arbitration provisions are unenforceable.

Piper's Account Agreements are Contracts of Adhesion

7. A contract of adhesion is a contract whose terms are dictated by one contracting party to another who has no voice in its formation. *Kloss* at paragraph 24, citing Corbin on Contracts, section 1.4 at 13 (1993).

8. "Contracts of adhesion arise when a standardized form of agreement, usually drafted by the party having superior bargaining power, is presented to a party, whose choice is either to accept or reject the contract without the opportunity to negotiate its terms." *Kloss*, 2002 MT 129 ¶ 24 (quoting *Passage v. Prudential Bache Securities, Inc.* (1986), 223 Mont. 60, 66, 727 P.2d 1298, 1301-02 (citations omitted)).

9. In *Passage v. Prudential-Bache Securities, Inc.* (1986), 223 Mont. 60, 727 P.2d 1298, the Montana Supreme Court described contracts of adhesion in the Securities context and the circumstances under which they are unenforceable as follows:

> . . . [T]he investor is faced with an industry wide practice of including Arbitration Clauses in standardized brokerage contracts. As the investor faces the possibility of being

> excluded from the securities market unless he accepts a contract with such an agreement to arbitrate, such clauses come within the adhesion doctrine. However, mere inequality in bargaining power does not render a contract unenforceable, nor are all standardized contracts unenforceable. As a consequence of current commercial realities, form forum clauses will control, absent a strong showing it should be set aside. For such a contract or clause to be void, it must fall within judicially imposed limits of enforcement. It will not be enforced against the weaker party when it is: (1) not within the reasonable expectations of said party or (2) within the reasonable expectations of the party, but, when considered in its context, is unduly oppressive, unconscionable, or against public policy. [Citations omitted.]

10. In contracts of adhesion, the contract terms are "dictated by one party to another who has no bargaining power and no realistic options." *Kloss,* 2002 MT 129 ¶24. If the party in the lesser bargaining position has no meaningful opportunity to negotiate or reject the terms of a contract, the contract is one of adhesion. *See Circuit City v. Mantor,* 335 F.3d 1101 (9th Cir. 2003) (applying California law).

11. "A meaningful opportunity to negotiate or reject the terms of a contract must mean something more than an empty choice. *At a minimum, a party must have reasonable notice of his opportunity to negotiate or reject the terms* of *a contract, and* he must have an actual, meaningful, and reasonable choice to exercise that discretion." *Circuit City v. Mantor,* 335 F.3d 1101, 1106 (9th Cir. 2003) (applying California law). (emphasis added).

12. Based upon the above Findings of Fact, Piper's account agreements are determined to be contracts of adhesion.

Piper's Pre-Dispute Arbitration Provision is Unconscionable

13. In *Kloss* the Court set forth the following eight factors which this Court must examine in determining the issue of the conscionability of Piper's pre-dispute arbitration provision:

    1. Are potential arbitrators disproportionately employed in one or the other party's field of business?

    2. Do arbitrators tend to favor "repeat players" as opposed to workers or are unlikely to be involved in arbitration again? In other words, is there a tendency by arbitrators to avoid decisions which will result in the loss of future contracts for their services?

    3. What are the filing fees for arbitration compared to the filing fees in Montana's district courts?

    4. What are arbitrators' fees? Do they make small claims prohibitive? Do they discriminate against consumers or workers of modest means?

    5. Are arbitration proceedings shrouded in secrecy so as to conceal illegal, oppressive or wrongful business practices?

    6. To what extent are arbitrators bound by the law?

7. To what extent are arbitrators bound by the facts?

8. What opportunity do claimants have to discover the facts necessary to prove a claim such as a company's business practices?

14. Based upon the above Findings of Fact, the Court finds that Piper's pre-dispute arbitration provision is unconscionable and therefore unenforceable.

Piper's Pre-Dispute Arbitration Provision Was Not Within The Plaintiff's Reasonable Expectations

15. Based upon the above Findings of Fact the Court concludes that Mr. Willems' reasonable expectation when signing Exhibit A was to protect his mother by placing his name on her account. Mr. Willems' reasonable expectations did not include agreeing to binding arbitration of disputes concerning his IRA account which is the subject of this litigation.

16. Based upon the above Findings of Fact the Court concludes that Mr. Willems' reasonable expectation in signing Exhibit B was to establish a conservative money market account with his wife. These expectations had nothing to do with his IRA. Therefore, Mr. Willems did not reasonably expect that by signing Exhibit B he was agreeing to binding arbitration of disputes concerning his IRA which is the subject of this litigation.

Piper Has Failed to Demonstrate that the Plaintiff Voluntarily, Knowingly, and Intelligently Waived His Constitutional Rights to a Jury Trial and Access the Courts

17. The right of trial by jury is secured to all and shall remain inviolate. Article II, Section 26, Montana Constitution. This constitutionally guaranteed right is fundamental and deserving of the highest level of court scrutiny and protection. *State v. LaMere,* 2000 MT 45, 298 Mont. 358, 2 P.3d 204.

18. Courts of justice shall be open to every person and speedy remedy afforded for every injury to person, property, or character. Article II, Section 16 Montana Constitution. This right is as fundamental as any other Article II right because the right of access to the courts is included within the Constitution's Declaration of Right and without the right to access the courts other Article II rights would have little protection from infringement, and, thus, little meaning. *Kloss,* supra (Nelson, J. concurring) at ¶ 57.

19. Constitutional rights that cannot be enforced are illusory. *Id.* at ¶ 58.

20. A waiver of a fundamental right must be proven to have been made voluntarily, knowingly and intelligently – typically by the party seeking the waiver. *Id.* at ¶ 64.

ORDER

Based upon the Findings of Fact herein, the Court finds that Piper has failed to demonstrate a voluntary, knowing, and intelligent waive by the Plaintiff of his constitutional rights.

Accordingly, it is hereby

ORDERED that the Defendant's Motion to Compel Arbitration and Stay Proceedings is DENIED.

DATED this 7th day of April, 2004.

/s/ Kurt Krueger
KURT KRUEGER
District Court Judge

Piper Jaffray Self-directed IRA

APPLICATION

PIPER JAFFRAY

* * *

C. ACCEPTANCE, ARBITRATION AGREEMENT AND SIGNATURE . . .

(4) The Customer Agrees to Arbitrate:

- **Arbitration is final and binding on the parties.**
- **The parties are waiving their right to seek remedies in court, including the right to jury trial.**
- **Pre-arbitration discovery is generally more limited than and different from court proceedings.**
- **The arbitrators' award is not required to include factual findings or legal reasoning and any party's right to appeal or to seek modification of rulings by the arbitrators is strictly limited.**
- **The panel of arbitrators will typically include a minority of arbitrators who were or are affiliated with the securities industry.**

I agree to arbitrate any disputes between Piper Jaffray and me. I specifically agree and recognize that all controversies which may arise between Piper Jaffray, its agents, representatives or employees and me, concerning any transaction, account or the construction, performance or breach of this or

any other agreement between Piper Jaffray and me, whether entered into prior, on, or subsequent to the date hereof, shall be determined by arbitration to the full extent provided by law. Such arbitration shall be in accordance with the rules then in effect, of the Arbitration Committee of the New York Stock Exchange, Inc. or the National Association of Securities Dealers, Inc. as I may elect. I authorize Piper Jaffray, if I do not make such election by registered mail addressed to Piper Jaffray at its main office within 15 days after receipt of notification from Piper Jaffray requesting such election, to make such election on my behalf. However, it is understood, no person shall bring a putative or certified class action to arbitration, nor seek to enforce any pre-dispute arbitration agreement against any person who has initiated in court a putative class action; who is a member of a putative class who has not opted out of the class with respect to any claims encompassed by the putative class action until: (i) the class certification is denied; (ii) the class is decertified; or (iii) the customer is excluded from the class by the court.

Such forbearance to enforce an agreement to arbitrate shall not constitute a waiver of any rights under this agreement except to the extent stated herein.

PAT Plus Account

CO-OWNER AGREEMENT

PIPER JAFFRAY

Customer Copy

* * *

12. Customer Agrees to Arbitrate.

- **Arbitration is final and binding on the parties.**
- **The parties are waiving their right to seek remedies in court including the right to jury trial.**
- **Pre-arbitration discovery is generally more limited than and different from court proceedings.**
- **The arbitrators' award is not required to include factual findings or legal reasoning and any party's right to appeal or seek modification of rulings by the arbitrators is strictly limited.**
- **The panel of arbitrators will typically include a minority of arbitrators who were or are affiliated with the securities industry.**

You agree to arbitrate any disputes between Piper Jaffray and you. You specifically agree and recognize that all controversies which may arise between Piper Jaffray, its agents, representatives or employees and you concerning any transaction, account or the construction, performance or breach of this or any other agreement between us, whether entered into prior, on, or subsequent to the date hereof, shall be determined by arbitration to the full extent

provided by law. Such arbitration shall be in accordance with the rules then in effect of the Arbitration Committee of the New York Stock Exchange, Inc. or the National Association of Securities Dealers, Inc. as you may elect. You authorize Piper Jaffray, if you do not make such election by registered mail addressed to Piper Jaffray at its main office within 15 days after receipt of notification from Piper Jaffray requesting such election, to make such election on your behalf.

However, it is understood, no person shall bring a putative or certified class action to arbitration, nor seek to enforce any pre-dispute arbitration agreement against any person who has initiated in court a putative class action; who is a member of a putative class who has not opted out of the class with respect to any claims encompassed by the putative class action until:

(i) the class certification is denied;

(ii) the class is decertified; or

(iii) the customer is excluded from the class by the court.

Such forbearance to enforce an agreement to arbitrate shall not constitute a waiver of any rights under this agreement except to the extent stated herein.

CASE STATUS AS OF 12/07/05

Plaintiff	MT Supreme Court Docket No.	Disposition
Terri A. Bagley v. U.S. Bancorp Piper Jaffray Inc., et al.	Case No. 04-446	Appeal dismissed after mediation
Vicki Berryman v. U.S. Bancorp Piper Jaffray Inc., et al.	Case No. 04-585	Petition for Writ of Certiorari Denied, No. 05-86
Sandra Brown v. U.S. Bancorp Piper Jaffray Inc., et al.	Case No. 04-447	Appeal dismissed after mediation
John P. and Audrey Daly v. U.S. Bancorp Piper Jaffray Inc., et al.	Case No. 04-490	Petition for Writ of Certiorari Denied, No. 05-86
Roberta J.Emett/Kathleen E. Merrett v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-517	Petition for Writ of Certiorari Denied, No. 05-86
Estate of Alice A. Franey U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-493	Petition for Writ of Certiorari Denied, No. 05-86
Joseph Froehlich, et al. v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-495	Settled at mediation/to be dismissed
Raymond Kaufman, et al. v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-491	Petition for Writ of Certiorari Pending, No 05A199
James Leary v. U.S. Bancorp Piper Jaffray Inc., et al.	Case No. 04-448	Petition for Writ of Certiorari Denied, No. 05-86
Suzanne McGee v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-494	Appeal dismissed after mediation
Margaret McGrath v. U.S. Bancorp Piper Jaffray Inc., et. al.		Dismissed after mediation but before appeal filed
Debbie Mueller v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-530	Appeal dismissed after mediation
Mike Paffhausen v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-449	Pending in MT Sup. Ct.
Juanita Periman v. U.S. Bancorp Piper Jaffray Inc., et al.	Case No. 04-450	Settled at mediation/to be dismissed
Evelyn Pickett v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-533	Settled at mediation/to be dismissed
John D. Shea and Brenda Shea v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-451	Petition for Writ of Certiorari Denied, No. 05-86
James and Brenda Shea v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-532	Appeal dismissed after mediation
James Staedt v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-492	Appeal dismissed after mediation
Stephen C. Tomazich v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-452	Affirmed by MT Sup. Ct.
Robert and Sheryl Tremis v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-453	Appeal dismissed after mediation
Shirley A. Turley v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-431	Settled at mediation/to be dismissed
Harry Willems v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-454	Affirmed, then dismissed as a result of mediation
Nancy Zigrang v. U.S. Bancorp Piper Jaffray Inc., et. al.	Case No. 04-455	Remanded by MT Sup. Court for further findings

No. 05-745

Supreme Court, U.S.
FILED
JAN 10 2006
OFFICE OF THE CLERK

In The
Supreme Court of the United States

PIPER JAFFRAY & CO., et al.,

Petitioners,

v.

RAYMOND KAUFMAN, Individually and as Trustee of the MONTANA FACIAL SURGERY PENSION AND PROFIT PLAN and JANET L. NOTHSTINE,

Respondents.

On Petition For Writ Of Certiorari To The Montana Supreme Court

BRIEF IN OPPOSITION

WILLIAM P. JOYCE
JOYCE, JOHNSTON & MACDONALD
321 W. Galena, Suite B
Butte, Montana 59701
(406) 723-8700

Attorneys for Raymond Kaufman, Individually and as Trustee of the Montana Facial Surgery Pension and Profit Plan and Janet L. Nothstine

COCKLE LAW BRIEF PRINTING CO (800) 225-6964
OR CALL COLLECT (402) 342-2831

QUESTION PRESENTED

Should this Court review the decision of the Montana Supreme Court in which the Montana court simply followed the dictates of the Federal Arbitration Act according to its express terms by applying state fiduciary duty law?

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
TABLE OF AUTHORITIES	iii
STATEMENT OF THE CASE	1
SUMMARY OF ARGUMENT	2
REASONS FOR DENYING PETITION FOR CERTIORARI	3
CONCLUSION	11

TABLE OF AUTHORITIES

Page

CASES:

Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265 (1995) 3, 4

Amoco Prod. Co. v. Charles B. Wilson, Jr. Inc., 266 Kan. 1084, 976 P.2d 941 (Kan. 1999) 8

Appeal of Concerned Corporators of Portsmouth Sav. Bank, 129 N.H. 183, 525 A.2d 671 (N.H. 1987) 8

Aronson v. Quick Point Pencil Co., 440 U.S. 257 (1979) 3, 5

Brown v. Halbert, Division Three, 271 Cal. App. 2d 252, 76 Cal.Rptr. 781 (Cal.App. 1969) 8

Chor v. Piper, Jaffray & Hopwood, Inc., 261 Mont. 143, 862 P.2d 26 (1993) 6, 7

Deist v. Wacholz, 208 Mont. 207, 678 P.2d 188 (1984) 7, 9

Ditis v. Ahlvin Const. Co., 408 Ill. 416, 97 N.E.2d 244 (Ill. 1951) 8

Doctor's Associates, Inc. v. Casarotto, 517 U.S. 681 (1996) 4

Ellezy v. Fyr-Pruf, Inc., 376 So. 2d 1328 (Miss. 1979) 9

Erie R. Co. v. Tompkins, 304 U.S. 64 (1938) 3

In re Evans, 113 Ariz. 458, 556 P.2d 792 (Ariz. 1976) 8

Kingston v. Ameritrade, Inc., 2000 MT 269, 302 Mont. 90, 12 P.3d 929 6

Kitchen Krafters Inc. v. Eastside Bank of Montana, et al., 242 Mont. 155, 789 P.2d 567 (1990) 6

TABLE OF AUTHORITIES – Continued

Page

Kloss v. Edward D. Jones & Co., 2002 MT 129, ¶ 37, 310 Mont. 123, 54 P.3d 1 ..... 5, 6, 8

Lindsay v. Marcus, 137 Colo. 336, 325 P.2d 267 (Colo. 1958) 8

Meinhard v. Salmon, 249 N.Y. 458, 164 N.E. 545 (1928) 8, 9

Murphy v. Redland, 178 Mont. 296, 583 P.2d 1049 (1978) 7

Perry v. Thomas, 482 U.S. 483 (1987) 3, 4

Ruhlin v. New York Life Ins. Co., 304 U.S. 202 (1938) 10

Scherk v. Alberto-Culver Co., 417 U.S. 506 (1974) 4

Silverman v. Bresnahan, 35 N.J. Super. 390, 114 A.2d 307 (N.J. 1955) 8

Van Stee v. Ransford, 346 Mich. 116, 77 N.W.2d 346 (Mich. 1956) 8

Volt Information Sciences, Inc. v. Board of Trustees of Leland Standford Junior University, 489 U.S. 468 (1989) 4

Watson v. Fultz, 239 Mont. 364, 782 P.2d 361 (1989) 6, 9

Willems v. US Bancorp Piper Jaffray, Inc., et al., 2005 MT 37, 326 Mont. 103, 107 P.3d 465 ..... *passim*

Young v. Field, 548 So.2d 784 (Fla. 1989) 8

STATUTES

Section 27-5-114(2) MCA (2003) 10

TABLE OF AUTHORITIES – Continued

Page

OTHER AUTHORITIES:

9 U.S.C. § 2, Federal Arbitration Act (FAA) 3, 4, 5, 10

STATEMENT OF THE CASE

Respondents Raymond Kaufman, Janet L. Nothstine and the Montana Facial Surgery Pension and Profit Plan are among 23 victims of US Bancorp Piper Jaffray Inc., Piper Jaffray, Inc., Robert English ("Piper"), and Thomas J. O'Neill's unethical and deceitful securities practices which were initially discovered and litigated by the Securities Department of the Office of the State Auditor of Montana. Respondents filed their Complaint against Piper alleging that, *inter alia*, Piper embarked upon a fraudulent scheme with regard to Respondents' retirement or life savings accounts. The Respondents litigated the question of arbitration in the District Court and on appeal to the Montana Supreme Court. On August 9, 2005 the Montana Supreme Court affirmed the lower denial of Piper's Motion to Compel Arbitration in an unpublished opinion (App. 1-5). Significantly, this Petition for a Writ of Certiorari follows a similar Petition which was filed on July 13, 2005 styled *Piper Jaffray & Co., et al. v. John D. Shea, et al.* (Cause No. 05-86) which also involved the 23 cases dealing with Piper and its broker Thomas J. O'Neill.

Further, the decision for which Piper has filed this Petition for Certiorari and the decisions for which Piper filed it previous Petition for Certiorari in *Shea*, all incorporate the reasoning of the Montana Supreme Court in *Willems v. US Bancorp Piper Jaffray, Inc., et al.*, 2005 MT 37, 326 Mont. 103, 107 P.3d 465 (decided February 22, 2005) (App. 37-49).[1] Piper is therefore seeking a second

[1] *Willems* had been settled in principal by Piper Jaffray shortly before the opinion was issued before the parties had moved to dismiss the appeal as moot. As a result, *Willems* is not one of the cases for which review by this Court may be sought.

review of the *Willems* decision. Although Piper advances a slightly different rationale, in substantive terms, it again seeks to re-argue the attack on *Willems* it advanced in *Piper Jaffray & Co., et al. v. Shea, et al.* (Cause No. 05-86). The Petition in *Piper Jaffray & Co. v. Shea* was denied by this Court on October 31, 2005. Because the arguments for denying the Writ in this case are identical to the basis for denying the Writ in *Shea* the arguments are reproduced here.

SUMMARY OF ARGUMENT

Certiorari is not appropriate in the instant case for the same reasons it was not appropriate in the case of *Piper Jaffray & Co. v. Shea* – namely, that no federal question was addressed by the Montana court; rather, the court clarified the scope of the fiduciary duty which arose under state law from the unique factual circumstances of this case. Moreover, even if a federal question is implicated, this Court should decline to exercise its discretion in granting review because compelling reasons do not exist for certiorari in this fact-driven case where Piper, at best, seeks to challenge the state court's application of the facts to the law. The Montana Supreme Court simply applied Montana state law regarding the duty of a fiduciary to the Respondents in this case. Because Piper fell short of that duty, the Montana Supreme Court appropriately found Piper's arbitration provision to be unenforceable. Having appropriately applied Montana law regarding fiduciary duties to these brokerage accounts, and in compliance with the express provisions of the Federal Arbitration Act requiring states to apply state law, certiorari is not appropriate. This is a simple, unpublished state law matter of

no precedential value beyond its peculiar facts. Piper has attempted to dress up the issue as a federal one, which it decidedly is not.

REASONS FOR DENYING PETITION FOR CERTIORARI

Section 2 of the Federal Arbitration Act (FAA) provides that written arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of *any* contract." 9 U.S.C. § 2. This provision of the FAA "provides the touchstone for choosing between state-law principles and principles of federal common law envisioned by the passage of that statute." *Perry v. Thomas*, 482 U.S. 483, 492, n.9 (1987). "An agreement to arbitrate is valid, irrevocable, and enforceable, *as a matter of federal law*. . . . State law, whether of legislative or judicial origin, is applicable *if* that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally." *Id.* "States may regulate contracts, including arbitration clauses, under general contract law principles and they may invalidate an arbitration clause 'upon such grounds as exist at law or in equity for the revocation of *any* contract.'" *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265 (1995).

This principle comports with the general rule that contract law is typically the domain of the state. *See Aronson v. Quick Point Pencil Co.*, 440 U.S. 257, 262 (1979); *Erie R. Co. v. Tompkins*, 304 U.S. 64, 78 (1938). Thus, generally applicable state law contract defenses, such as fraud, duress, or unconscionability, may be applied

to invalidate arbitration agreements without contravening Section 2 of the FAA. *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681, 687 (1996). In short, state law governs contract formation and revocation questions, and also is applied to determine questions of validity. *Id.*

What States may not do is invalidate arbitration agreements under state laws applicable only to arbitration agreements. *Doctor's Associates, Inc.*, 517 U.S. at 687 (citing *Allied-Bruce*, 513 U.S. at 281; *Perry*, 482 U.S., at 492, n. 9). "By enacting § 2, Congress precluded States from singling out arbitration provisions for suspect status, requiring instead that such provisions be placed 'upon the same footing as other contracts.'" *Id.* (*citing Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 511 (1974)). In fact, one of the fundamental tenets of the FAA is that arbitration provisions should exist "upon the same footing" as all other provisions in a contract. *Volt Information Sciences, Inc. v. Board of Trustees of Leland Standford Junior University*, 489 U.S. 468, 474 (1989).

The issues presented herein arise under state law. Piper identifies no Montana state laws applicable only to arbitration agreements which would invoke federal jurisdiction, or require the application of federal law. Nor did the Montana court in the lead case of *Willems*[2] identify any such law singling out arbitration agreements. Rather, the Montana court applied state laws to find that a fiduciary

[2] The *Willems* case itself is not strictly before the Court because the parties reached a settlement after the case was remanded to the District Court. However, as set forth in the Statement of the Case section the Montana Supreme Court relied on the analysis in *Willems* in issuing non-published opinions in the six cases presently before the Court on Piper's Writ of Certiorari.

duty arose between the broker and the investors herein. This duty arose NOT from the arbitration provision contained in the contract, but from the contract provision which granted Piper control to buy, sell and trade securities in the investors' accounts whenever Piper, in its discretion, deemed it necessary or appropriate. *Willems*, *supra*, ¶ 25 (App. 47.). Thus, the *Willems* holding itself has less to do with arbitration than it has to do with the scope of the fiduciary duty under Montana law. This is a matter that is appropriately left to the individual states under our federal system. *See, e.g., Aronson*, 440 U.S. at 262. Because the Montana Court applied general principles of state law, and did not single out the arbitration agreement, review by this Court upon a writ of certiorari is not warranted.

In fact, the Montana court expressly identified the FAA provision (and the identical state counterpart), and applied state law as required by that Act. In the lead case of *Willems*, the Montana Court expressly recognized the dictates of the FAA[3] when it held:

> We conclude that the District Court created no new special legal standards but instead properly applied Montana case law by relying on *Kloss*. The FAA provides that an agreement to arbitrate is valid except where grounds exist at law or in

[3] 9 U.S.C. § 2 provides: "A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

> equity to revoke the contract . . . Montana law also requires the enforcement of predispute arbitration clauses except upon grounds that exist at law or in equity for the revocation of a contract. *Kingston v. Ameritrade, Inc.*, 2000 MT 269, 302 Mont. 90, 12 P.3d 929.

Willems, at ¶ 27 (App. 48) (emphasis added).[4]

In *Willems*, the Montana court reviewed the provision in the Piper contracts which provided: "whenever Piper Jaffray deems it necessary for its protection, Piper Jaffray is authorized (but is not required) to: . . . Purchase, sell, assign, receive and deliver all or any part of the securities held or carried for you."[5] *Willems*, at ¶ 17 (App. 43). Under Montana law, "a fiduciary relationship is created whenever a broker has discretion to buy, sell, or otherwise control a client's account." *Willems,* at ¶ 14 (App. 42) (*citing Chor v. Piper, Jaffray & Hopwood, Inc.* (1993), 261 Mont. 143, 153, 862 P.2d 26, 32). Thus, this general contract provision, having nothing to do with arbitration, created a fiduciary duty. Under Montana law, a fiduciary must make full disclosure of all facts relevant to the transaction and relationship between the parties. *See, e.g., Kitchen Krafters Inc. v. Eastside Bank of Montana, et al.*, 242 Mont. 155, 163, 789 P.2d 567, 571 (1990); *Watson v. Lultz*, 239 Mont. 364, 368, 782 P.2d 361, 363 (1989).

---

[4] *Kloss v. Edward D. Jones & Co.*, 2002 MT 129, ¶ 37, 310 Mont. 123, 54 P.3d 1.

[5] Piper's contentions that the agreement's language granting broker discretion is standard in the industry was not presented below or considered or ruled upon by the Montana Supreme Court. Although it is irrelevant to the issues before this Court, Respondents are not waiving their right to oppose this contention.